THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS

UNDEPRECIATED INVESTMENT AS A UTILITY RATE BASE

GEORGE C. MATHEWS

THE REAL ESTATE CODE OF ETHICS

HERBERT U. NELSON

RELATIONSHIPS OF LANDLORDS TO FARM TENANTS

F. A. BUECHEL

PUBLIC UTILITY FINANCING, 1919-1925

HERBERT B. DORAU

THE UNIFORM ACCOUNTING SYSTEMS ADVOCATED BY UTILITY COMMISSIONERS

HIRAM T. SCOVILL

VOLUME I NUMBER 3 JULY 1925 PRICE $1.25 A COPY

In Chicago

THIS Bank underwrites and distributes high grade utility and real estate bond issues—and acts as Trustee, Transfer Agent and Registrar of Corporation Securities.

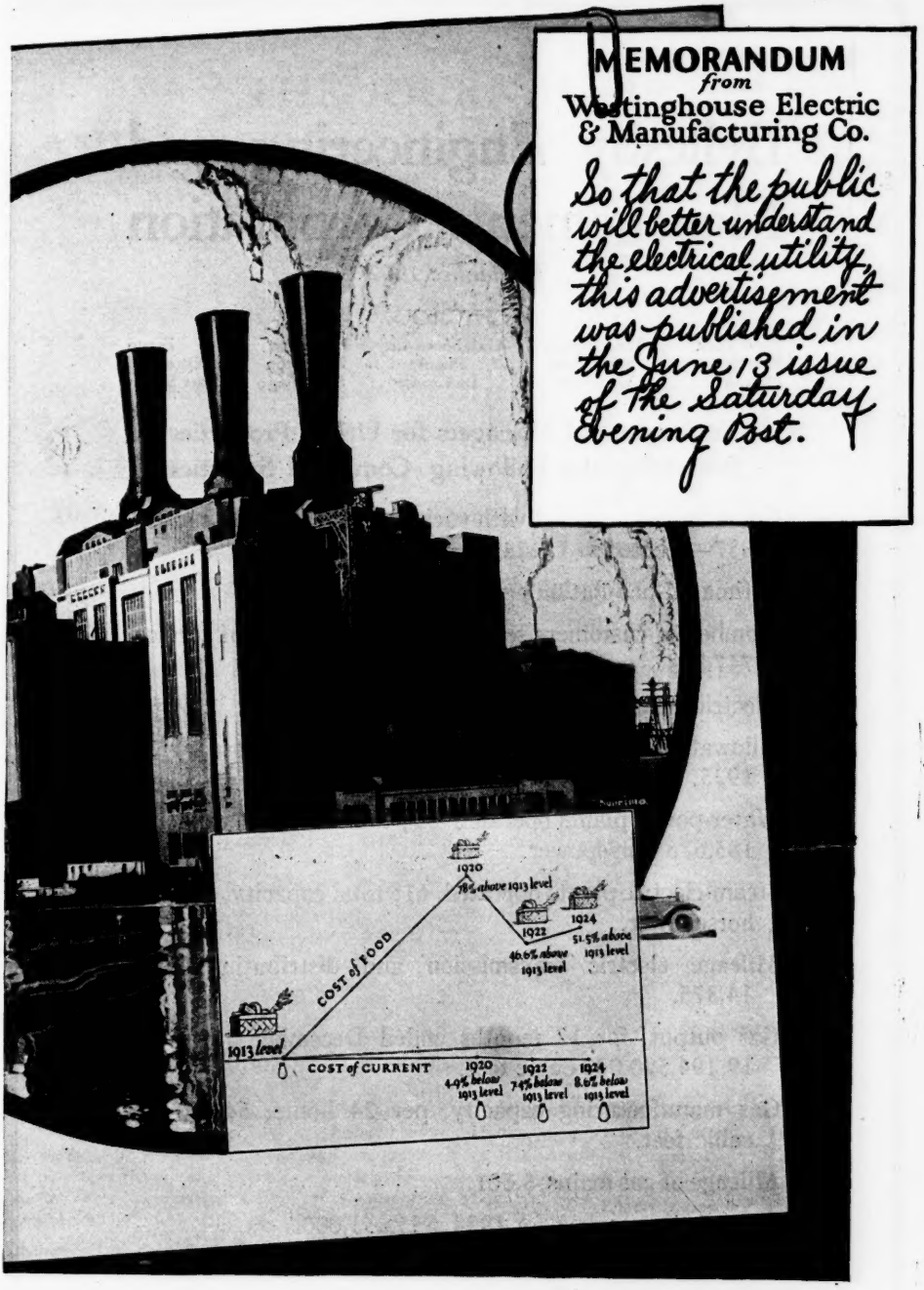
1869 UNION TRUST COMPANY 1925

FREDERICK H. RAWSON, *Chairman of the Board*
HARRY A. WHEELER, *President*

UNION TRUST COMPANY

One of Chicago's Oldest and Most Favorably Known Commercial Banks

JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS – Entered as second-class matter January 5, 1925, at the post-office at Chicago, Illinois, under the Act of March 3, 1879. Terms: $5 a year; single copies $1.25. Published quarterly for the Institute for Research in Land Economics and Public Utilities by A. W. Shaw Company, Cass, Huron and Erie Streets, Chicago, Illinois.


MEMORANDUM
from
Westinghouse Electric
& Manufacturing Co.
So that the public will better understand the electrical utility, this advertisement was published in the June 13 issue of the Saturday Evening Post.
1920
78% above 1913 level
1922
40.6% above 1913 level
1924
51.5% above 1913 level
COST of FOOD
1913 level
COST of CURRENT
1920
4.9% below 1913 level
1922
7.4% below 1913 level
1924
8.6% below 1913 level

THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS

CONTENTS FOR JULY, 1925

Undepreciated Investment as a Utility Rate Base	GEORGE C. MATHEWS	257
The Real Estate Code of Ethics	HERBERT U. NELSON	270
The Uniform Accounting Systems Advocated by Utilities Commissioners	HIRAM T. SCOVILL	276
A Challenge—to the Public? or to the Real Estate Business?	JOHN D. BLACK	292
Practical Policies of Land Colonization	B. F. FAAST	300
Public Utility Financing, 1919-1925	HERBERT B. DORAU	305
The Public Leasehold System in the United States	MARY L. SHINE	322
Relationships of Landlords to Farm Tenants	F. A. BUECHEL	336
The Public Control of House Rents	MARCUS WHITMAN	343
Department Contents		362
Book Reviews		363
Summaries of Research		371
Comments on Legislation and Court Decisions		375

Subscription Rates: $5 a year; $1.25 a copy. Remittances may be made by personal checks, drafts, post-office or express money orders, payable to A. W. Shaw Company, Chicago.

Entered as second-class matter January 5, 1925, at the post-office at Chicago, Illinois, under the Act of Congress of March 3, 1879. Printed in the United States of America.

Editorial Correspondence: Letters regarding editorial matters should be addressed to the Editor, Sterling Hall, Madison, Wisconsin.

Business Communications: Letters concerning subscriptions or advertising should be addressed to A. W. Shaw Company, Chicago. Advertising rates furnished on application.

PUBLISHED QUARTERLY FOR THE INSTITUTE FOR RESEARCH IN LAND ECONOMICS AND PUBLIC UTILITIES, BY A. W. SHAW COMPANY, CASS, HURON AND ERIE STREETS, CHICAGO

THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS

RICHARD T. ELY
Editor-in-Chief

E. W. MOREHOUSE
Managing Editor

THE CONTRIBUTORS TO THIS NUMBER INCLUDE

George C. Mathews, Director, Statistical and Securities Division, Railroad Commission of Wisconsin.

Herbert U. Nelson, Executive Secretary, National Association of Real Estate Boards.

Hiram T. Scovill, Professor of Accountancy, University of Illinois.

John D. Black, Chief of Division of Agricultural Economics, University of Minnesota.

B. F. Faast, President, Wisconsin Colonization Company, Eau Claire and Chippewa Falls, Wisconsin.

Herbert B. Dorau, Research Instructor, Institute for Research in Land Economics and Public Utilities.

Mary L. Shine, Research Associate in the Institute.

F. A. Buechel, Head, Agricultural Administration, Agricultural and Mechanical College of Texas.

Marcus Whitman, Henry Strong Research Fellow in the Institute.

Martin G. Glaeser, Research Associate in the Institute.

B. H. Hibbard, Professor of Agricultural Economics, University of Wisconsin, and Research Associate in the Institute.

Gertrude Harley, Graduate Student in Land Economics, University of Wisconsin.

G. S. Wehrwein, Research Associate in the Institute.

W. G. Maas, Student, University of Wisconsin.

O. M. Johnson and B. W. Allin, Assistants in Agricultural Economics, University of Wisconsin.

E. W. Morehouse, Research Instructor in the Institute.

THE JOURNAL OF
LAND & PUBLIC UTILITY
ECONOMICS

JULY
1925

VOLUME I
NUMBER 3

UNDEPRECIATED INVESTMENT AS A UTILITY RATE BASE

By GEORGE C. MATHEWS

THE theory of proper regulation of utility rates may be expressed in very simple terms. Under normal conditions the utility is entitled to establish such rate schedules as will yield a fair return upon the fair value of its property. Administrative practice and the divergent views held by courts of appeal, however, have made the application of this seemingly simple rule complex and difficult.

The most difficult questions are those concerned with the determination of a proper rate base with reference to which the fair return is calculated. Among those questions two stand out as representative of the sharply divergent points of view that so frequently characterize controversies concerning valuation. These two issues, which are at the same time fundamental in the valuation problem, are (1) whether the investment standard or the cost-of-reproduction standard should be given greater weight in determining values for rate-making purposes, and (2) whether or not depreciation reserves should be deducted from the rate base, and if so, how much should be deducted. In the following discussion of these two issues, particular attention will be given to the propriety of using undepreciated investment as a rate base. The angle of approach throughout will be the financial point of view.

I. The Issue of Valuation Standards

The administrative public service commission is charged with the responsibility of applying the rules of fair dealing to the public utility; but, with courts of review holding widely different views as to what constitutes fair treatment, the regulating commission is left without definite standard or rule to guide its actions so that they may be in accordance with correct principles. An

example based on conditions faced by the Wisconsin Commission may serve to illustrate. The Supreme Court of Wisconsin, upon an appeal taken by the Waukesha Gas and Electric Company,[1] upheld a valuation made by the commission in which no addition had been made to actual investment to reflect post-war price levels. Although the court recognized that elements determinative of value, such as those mentioned in *Smyth* v. *Ames*,[2] must be considered, controlling weight was given to the actual investment.

In contrast to this decision is the recent opinion of a United States District Court in the Mobile gas case[3] wherein it was held in effect that reproduction cost at the date of the inquiry, rather than investment or original cost, was *the* important factor in valuation. We have also the able, but, from the standpoint of the commissions, unsatisfactory, decisions of the United States Supreme Court in the Southwestern Bell Telephone[4] and the Bluefield Water Works[5] cases. Unsatisfactory these decisions were bound to be because, after all, they merely restated elements which must be considered in determining value, without giving much indication of what weight, in the court's mind, should be given to each element or even as to which elements are most important.

Conclusions may be drawn from these decisions of the Supreme Court to support views of the valuation problem which seem almost irreconcilable. Advance reports quote Judge Winslow of the United States District Court for the southern district of New York, in an opinion rendered April 23, 1925, in the $1 rate case of the Consolidated Gas Company, as referring to reproduction cost less proved depreciation as the dominant element in determining a rate base. Reference has already been made to a similar opinion in the Mobile gas case.

Yet some of the state commissions have not interpreted the language of the Supreme Court as requiring the virtual abandonment of investment or original cost as a measure of value. Advocates of both conclusions have been able to draw comfort from the decisions, but neither the commission, which holds to the original cost basis, nor the lower court, which swings to extreme recognition of reproduction cost, has been able to establish its position as fully as it might desire, by authority of the Supreme Court decisions.

Attitude of Public toward Investment Standard

The public is likely to look upon measurement of value by the use of cost of reproduction as a means of profit-taking, inconsistent with the status of a public utility as a regulated industry. During a period of rising prices, and especially when the increase has been as great as that since 1916, such a reaction from the public is a natural one, whether or not it is based upon a correct conception of utility property values. In the early railway cases the parties stood in opposite positions. The public insisted upon the use of cost of

[1] *Waukesha Gas and Electric Company* v. *Railroad Commission*, 181 Wis. 281, P. U. R. 1923 E, 634.

[2] *Smyth* v. *Ames*, 169 U. S. 466.

[3] *Mobile Gas Co.* v. *Patterson*, 293 Fed. 208, P. U. R. 1924 B, 644.

[4] *State ex rel Southwestern Bell Telephone Company* v. *Missouri Public Service Commission*, 262 U. S. 276, P. U. R. 1923 C, 193.

[5] *Bluefield Water Works and Improvement Company* v. *West Virginia Public Service Commission*, 262 U. S. 679, P. U. R. 1923 D, 11.

reproduction, rather than original cost, as a basic measure of value; the railways took the position that investment should be controlling.

Public regulation of utilities by administrative boards is bound to be political in character. In proper form it will not be partisan, nor subject to personal political influences, nor directed to accomplishing the ends of a political party. It is political, however, in the sense that it represents the public policy of the state, within constitutional limits. If that public policy is enlightened, regulation expressing it will be enlightened. If public policy is sound, the principles of regulation which express that policy will be sound.

Within recent years state commissions have been inclined to emphasize the importance of attaching primary weight, in valuation cases, to the actual, legitimate, and prudent original cost of the properties to be valued. The fact that this policy has been more or less closely adhered to during a time of high prices has caused the charge to be made, in some quarters, that the commissions were controlled by motives of expediency, and that they expressed, not a reasonable and proper public policy, but a popular demand, which was based neither upon sound economic principles nor upon enlightened public policy.

Adherence to original cost as a principal measure of value may have been due in some cases to the fact that it offered a present means of keeping rates at lower levels than could be maintained if values were determined by other means. State commissions could not be unmindful of the force of popular opinion antagonistic to increased rates. It is hardly fair, however, to conclude that commissions were forced by popular clamor to the adoption of a valuation policy which had only its appeal to prejudice to support it. Such a conclusion, if justified, would mean that state regulation of rates had seriously failed to maintain a fair attitude toward the utility business. Generally speaking, this charge has not been made and cannot be maintained.

Attitude of Utilities toward Investment Standard

By no means all of the utility companies have objected to a valuation method which stresses the importance of original cost. As an illustration, the experience of the Wisconsin Commission may be cited. Since this country's entry into the World War, that body has passed upon many more than a thousand applications of utilities and electric railways for authority to increase rates, in which several hundred companies were involved. The instances in which companies asked that their return be based upon values expanded to give weight to prices which were much higher than original costs have been so few as to constitute conspicuous exceptions. Surely a valuation method which has found such general acceptance among utility companies cannot be based only on expediency. There must have been reasons for the use of the method which commended themselves to the judgment of utility management.

It is true that in many of the cases referred to, the companies were more concerned with getting relief for their pressing needs than they were to secure immediately a full fair return upon the value of their properties. Those times are some years in the past, however. There has been time enough for a full trial on the merits, but the companies which then voiced no serious objection to rates being based upon original cost still seem to be content with such basis.

It is also true that among the applicants in these cases were many community-owned properties, to whose owners the return on their utility investment was of minor importance; but even after making allowance for all such cases, the fact remains that, with infrequent exceptions, the commercial companies, for whose owners the utility business was the principal or only business, have continued to accept without protest valuations based principally upon original cost. It may be interesting to note also that the exceptions were confined almost entirely to companies with heavy capitalization where expansion of values seemed to offer a convenient means, even if not a permanent one, of remedying an unsound financial structure.

No more than one instance is recalled in which a telephone company in Wisconsin has asked for findings of value reflecting present-day prices on pre-war construction. Neither the Bell system company, which has over half of the telephone business in the state, nor the strong commercial independent companies have tried to secure such value as a rate base. What has been true of the telephone companies has been true, with the exception previously referred to, of the electric, gas, and electric railway companies. It would seem, then, that we cannot support the view that the policy of giving preponderant weight to original cost in public utility valuations has been dictated by motives of expediency or that it has denied to the utilities relief which they had reason to expect. Although facts are not available as to the experience of other state commissions, the reasons which have led Wisconsin utilities to accept, almost without protest, the commission's method of fixing the rate base, have been such that it may be assumed that other regulatory bodies have had a like experience.

II. Justification of Investment Standard from Financial Point of View

We may turn, then, to an analysis of these reasons and to a consideration of the soundness of the conclusions to which they point. It may be accepted as a well-established principle of law, despite a lack of judicial uniformity in its application, that the value of a public utility property in a rate case must be a value as of the time of the investigation, and that an element to be considered in the finding of such value is the cost of reproduction at that time. If a lesser rate base is fixed by the state and accepted by the utilities, it must be because the use of that lower base appears to be in the interests both of the public and of the utilities. That the lower rates thus made possible are immediately in the public interest probably requires no demonstration. For the benefit to the utility we must look to the future.

Market value of a public utility property may not have much bearing on the situation, but attention should probably be called to what the market-value situation has been during a considerable part of the high-price period. For practical purposes, there may be said to be two measures of the market value of a utility. The first is the selling price of its securities; the second is the price at which the property would sell as a going concern to interests desiring to control the business. As to the second of these measures, the selling price of going public utility concerns is determined more by earning power, present or prospective, geographical location, and competition among purchasing companies to secure control of the field, than it is by physical valuation. This may seem inconsistent with the accomplishment of the purposes of regulation, but,

from observation of a very considerable number of such sales, it appears to be the truth.

Prices of public utility securities have not been greatly influenced by changes in the cost of reproduction, although if rates and earning power are to be based on such cost it appears only reasonable to expect that in the long run security values will be affected. In general, values of utility securities declined very greatly, almost at the same time that cost of reproduction increased to a point far beyond former levels. The same thing was true of industrial securities. Industrial concerns, however, have earning power that is not as closely related to any physical base as is the earning power of public utilities. Cost of reproduction in many industrials has only a very limited effect upon value. To a great extent, the valuation of public utilities is based upon original cost or upon cost of reproduction or other facts related to physical property, only because regulation makes necessary a measure of value differing from market value. Value, as measured by a sale price, does not change immediately or directly as cost of reproduction changes, and is affected by such changes only as earning power is affected.

Effect of Using Reproduction-Cost Standard in High-Price Period

What effect, then, will values based upon cost of reproduction have upon earning power? How will the modified earning power affect the stability of securities? What effect will this have upon the cost of obtaining capital, and, since the cost of capital is an element in the cost of service, how will it affect the customer of the utility?

To answer these questions it is necessary to understand the usual financial structure of a public utility. The business is to a large extent conducted on borrowed money. At the end of 1924 a group of gas and electric companies in Wisconsin, comprising all of the larger companies, had outstanding a long-term debt of over $147,000,000, preferred stock of over $52,000,000, and common stock of about $38,500,000. Over 60% of the securities were outstanding for money borrowed, and considerably less than 20% was common stock. That is, less than one-fifth of the capital was in a position to benefit from increased earnings or to suffer from a decrease, unless that decrease should be beyond any that might reasonably be anticipated. In individual companies the long-term debt approached 70% of the total, and the common stock was as low as 15%. A financial structure containing 60% of bonds and 20% each of preferred and common stock is not unusual, although some of the more conservative companies are working toward a structure of 50% in bonds and the other half divided equally between preferred and common stocks.

With only 20% of the securities in the form of common stock, the returns on 80% of the capital are limited to rates specified in the bonds or in the preferred stock certificates, except in the somewhat unusual case of participating preferred stock. Likewise, the extent of participation in the assets of the business upon payment of the bonds or retirement of the preferred stock, or upon liquidation, is covered by contract. Four-fifths of the capital is represented by securities whose holders have no chance of speculative profit and who should be removed, as far as possible, from the danger of speculative loss.

With this typical financial structure in mind, we may ask what the effect of the use of valuations based on cost of repro-

duction at current prices would be upon the stability of utility securities and upon their holders. During the past few years the cost of reproduction of utility properties has exceeded corresponding pre-war costs by from 50% to 100% and perhaps by even larger percentages for some classes of property. A large amount of property has been added at high prices, in greater proportion in the electrical and telephone utilities than in water, gas, or street-railway concerns. At the beginning of the high-price period, practically all of the investment, necessarily, had been made at much lower price levels. With only 20% of the capital structure composed of common stock, an increase of 60% in value of the property—a conservative increase if reproduction cost at current prices were to control in valuation—would multiply the property value back of that stock by four. The element of speculation would have become very important.

Use of Cost-of-Reproduction Standard during Falling Prices

Commissions have frequently called attention to the danger to which a consistent use of the current reproduction cost basis would lead if a period of marked decline of prices should be encountered. The criticism has sometimes been made that those charged with the duty of administering regulatory laws conjured up this danger to support them in a refusal to recognize high reproduction costs at a time when such recognition would have meant rather general rate increases. We cannot inquire into the mental processes of commissioners, but we can test the soundness of their argument by reference to actual conditions and to what may reasonably be expected as to price trends.

If reproduction cost were to decrease to a level 20% below investment, the property values back of common stock would be entirely wiped out by valuations based on current reproduction costs. It may be natural, at a time when high-price levels would make reproduction valuations immediately advantageous to the common stock, for the holders of such stock to feel that present advantages, real and tangible, more than offset the dangers which, after all, may not actually be encountered. What is to be expected in the way of future price levels we may leave for discussion by those who think they can forecast such levels. We know, however, that some of the elements in public utility construction have actually declined very much in cost. For some time past the price of copper, an important material in electrical construction, has hardly exceeded half of the price actually paid by some companies a few years ago. In some localities, at least, the labor cost of construction has decreased considerably, perhaps due as much to increased efficiency as to reduced wage rates. One of the large utility properties in Wisconsin was built entirely since 1917, part of it at prices higher than the present level.

Investment Standard Protects Capital

Leaders in the electrical industry estimate its capital requirements for the next decade at from $600,000,000 to $1,000,000,000 a year. If high prices continue for 10 years, there will be far more high-priced construction in the electrical and telephone systems than there will be property built at pre-war prices. With the certain demand for enormous amounts of capital during years in which no great recession of prices can now be anticipated, it is not

unreasonable to look for the time to come when valuations at then current reproduction costs will scale down actual, prudent, and necessary investment, perhaps so far as to wipe out all property values supporting the common stock, and even to depreciate that to which the holder of preferred stock looks for his protection. With utilities going further and further in the sale of preferred stock to customers, the effect of weakening the preferred stockholders' position may be even more serious than where the bondholders are affected, because the success of the whole undertaking is largely dependent on the attitude of the customer.

Up to the present time, the general situation is that increases which would result from application of current prices to pre-war construction more than offset the shrinkage resulting from placing such prices on property built at extremely high prices; but even now this situation is not universal and in a few years, if there should be any material decline in construction costs, it will not even be the usual one. If prices do not go to lower levels, utility capital will be safe in asking for valuations based on current prices. If prices do decline, and especially if that decline does not come for seven or eight years, invested capital will be impaired by such valuations. There seems to be sufficient prospect of eventual lowering of prices to justify the warning sounded by the public service commissions against a policy of inflating values to levels that may not be maintained if the method of valuation which produced the inflation is followed consistently. The wisdom of those companies which have not sought for values higher than original cost may yet be demonstrated, provided the investment basis can be followed consistently, regardless of current price levels.

Investment Standard and Cost of Capital

Not only does the investment basis seem to offer the best assurance of protection to capital, but the logic of the situation points toward a saving to the public in at least one important respect —the cost of the capital required for the business. If rates are to be so fixed as to yield a fair return on reproduction cost, the common stockholder's dividend will increase as prices rise, and fall as prices go down. If reproduction cost should be 20% less than investment, all that the common stockholder in a typical utility could receive would be the margin left after the interest and dividend payments on bonds and preferred stock had been taken out of a fair return on a value only equal to the investment of bond and preferred stockholders. A severe decline might leave the common stockholder with no earnings on his holdings.

The tendency of reproduction-cost valuations, unless we are prepared to assume that prices will not decline at all, must be to make the common stock's position a speculative one. If price changes are severe, such stock will be taken entirely out of the investment class. Although only very radical reductions could affect the security of the bondholder, it is entirely possible that the investment position of the preferred stock may be injured.

A utility which has consistently earned a substantial dividend on its common stock can borrow money more cheaply than one whose entire earnings are required for interest and preferred stock dividends. The security market is decidedly sensitive to such conditions. It is a difficult matter to measure the difference in interest rates from this cause, because of other complicating factors;

but that the difference does exist is within the knowledge of every public utility manager, of every investment banker, and of every public service commission.

The effect on cost of capital does not end with the bond interest rate. The dividend rate on preferred stock and the very possibility of preferred-stock financing is controlled largely by the amount of earnings above bare dividend requirements. In one rather small Wisconsin city, one of the local utilities, having a good record of earnings, recently sold to its customers a $500,000 issue of preferred stock with a 6½% dividend rate, with no solicitation other than a brief notice sent with the monthly service bills. In the same city another utility, not so favorably situated as to earnings, has for years been selling preferred stock carrying a higher dividend rate. This company has been using advertising rather freely, and yet its total sales have not approached $250,000. To refer to such situations is merely to state what all realize to be the truth, that the stability of a favorable earning position enables the industry to employ capital cheaply. Such stability can be secured only if the utility is permitted to earn a fair return upon a stable base, and no base can contain the elements of stability if it changes with every change of price levels.

Investment Standard and the Supply of Capital

Although it may not completely define what constitutes a fair return, the statement has frequently been made that a return is fair which promotes the free movement of capital into the public utility business. For that capital which ordinarily secures no part in management and has no possibility of speculative profit and which is free to enter the business or to go into other lines, it almost begs the question to say that a fair return is the element which controls investment in the utility business. For the common stock, the continuance over a period of years of a return adequate to produce for dividends and surplus the customary wage of capital similarly situated would be sufficient inducement to secure the flow of capital to the business, if such flow were not artificially controlled. No better proof of this need be offered than the increasingly wide distribution of the common stock of the American Telephone and Telegraph Company. Stability of values and of earning power was sufficient to create an ever-increasing demand for this stock before any recognition of enhanced values in rate cases. Although the American Telephone and Telegraph Company might well have the prospect of as great immediate and perhaps temporary gain as any other utility, by having values of all subsidiaries established upon current price levels, it required no such means to secure an adequate supply of capital for common-stock investment.

In many utility undertakings the opportunity for direct investment in common stock has been restricted by the necessity of keeping control in the hands of the holding company. Instead of the common stock being available for general public purchase, various debt issues and preferred stocks of holding companies are offered. Seemingly no demonstration is required to establish that stability of earnings and of underlying property values is hardly less important in attracting capital investment into such securities than it is in attracting it directly to investment in corresponding securities of operating companies.

Investment Standard and the Holding Company

There remains the question whether stability of earnings based on stable values will attract that portion of the capital represented in the control of the holding companies. Here we are dealing more or less with personal views of the investors. Such control may be, and often is, in the hands of a few individuals. The availability of this capital for the public utility business, if values are based upon original cost, will be controlled to greater or less degree by the attitude of a limited number of persons. There can be no question that in some holding companies the controlling capital has been attracted by the speculative possibilities associated with present price levels. It is true, also, that utility holding companies or, as some are self-styled, "investment" companies have developed enormously since the recent great increase of prices. It is equally true, however, that many of such companies were organized and furnishing capital to the utility business long before the possibility of speculative profit, resulting from increased prices, had appeared. There is no reason to believe that the important place occupied by the holding company would not have been filled if prices had stayed at pre-war levels, or, in other words, if a marked difference between original and reproduction costs had never developed. Neither do the facts seem to indicate that adherence to original cost in valuations would now prevent the free flow of capital into the utility business. Witness the situation of the American Telephone and Telegraph Company, previously referred to, and the fact that many large utilities have not sought to establish a rate base founded on present prices. Some individual capitalists might be missing from holding-company circles, but those companies that are most closely associated with establishing the industry in its present place would hardly be affected. Some of them would be left, as the result of valuation methods, exactly in the position they have voluntarily taken.

It is not the purpose of this paper to attempt to bridge the gap between the legal conception of fair value, a conception somewhat vague and incompletely stated, and the original-cost basis. It is hoped merely to point out certain advantages to customers and capital in as close adherence as the state of the law will permit, to original cost as a measure of the proper rate base. To the customer it should, in the long run, mean a lower rate for service, because the stability afforded to invested capital should make it possible to secure cheaper capital. To the investor in bonds or in preferred stock there should be an advantage in the very stability of values even when fluctuations in reproduction-cost valuations might not be severe enough to endanger the actual payment of interest or dividends. The common stockholder, if he represents capital which is devoted to building an industry for the purpose of making profits from its continued operation, will benefit from better assurance of sustained earnings. The speculative chance will be minimized but the stock should have a sound investment position. Many such stocks have that position today and in by no means all cases are their owners willing to jeopardize it.

Billions of dollars will be needed in the utility business. Whatever strengthens the permanent investment position of its securities or of those of its holding companies makes them more attractive to the millions of people who must supply the capital, reduces the cost

of money, and benefits all except the speculator—to whom, after all, a regulated business makes a poor appeal.

III. The Treatment of Depreciation

The title of this paper refers to the use of undepreciated investment as a rate base. Certain advantages of investment, or, more properly speaking, of original cost, over current reproduction cost, as a rate base, have been discussed. Such a rate base may not be value in the present judicial interpretation of that term. It is not the writer's purpose to speculate whether such cost might ever properly be used as value in such cases, for example, as those of municipal purchase of a utility business or property. Whether or not original cost, modified by proper recognition of such elements as going-concern value, can be construed to be "value" in the sense that that term is used in rate cases is also perhaps beyond the scope of this discussion. This standard will meet the test of producing the necessary capital, however, provided always that such elements as the value of the business, distinct from the value of physical property, are not ignored. If that capital is freely supplied as rapidly as needed by the industry, it is difficult to conclude that a fair return is denied. To the writer, therefore, a distinction seems possible between the legal idea of fair value and the business conception of a reasonable rate base, although this is not altogether easy to explain.

In what has been said thus far, no reference has been made to the effect of accrued depreciation upon the rate base. The attempt has been, rather, to outline the economic justification for the use of original rather than current reproduction cost, without reference to the effect of depreciation on either. What is said here as to the use of a rate base without deduction for depreciation applies equally to valuations based upon original cost and to those based upon current reproduction cost or upon any other level of prices.

Recognition of depreciation in the physical property of a utility has been quite general in court and commission decisions. Many of the leaders in the railroad and utility businesses, however, contend that, unless the properties have been neglected and current repairs deferred, there is no actual depreciation, that their properties can have an established business only when many parts have been in service for some time, that this is the condition for which the company builds, that such property furnishes service equal to, if not better than, that which could be furnished by a new property, and that it has not actually declined in value. Without attempting to determine the soundness of this position, it should probably be said that many utility men have been willing to back their conclusions by buying properties at prices which did not appear to reflect any accrued depreciation.

Recently some decisions of the lower federal courts have held, in effect, that there should be no deduction from the rate base on account of accrued depreciation or on account of the accumulation of reserves to meet retirement losses. There have also been a considerable number of commission decisions in which there was no direct reflection of either accrued depreciation or accumulated reserves in the rate base. This raises the question whether such decisions are not inconsistent with earlier cases in which a deduction for depreciation was sanctioned. The answer to this would appear to depend entirely on the conditions to which the seemingly conflicting doctrines have been applied.

Two Views of Depreciation Reserves

In order to make an intelligible attempt to reconcile these holdings, it becomes necessary to analyze two extreme views regarding the methods of providing, and the purposes to be served by, reserves for losses completely realized upon retirement of property. The first view, which approaches that usually reflected in accounting in manufacturing industries and that responsible for depletion allowances in industries consuming natural resources, is that there is an actual depreciation from the date of installation of a unit of property, rather closely proportionate to the ratio of elapsed life to total life expectancy of the unit, and that a reserve should be accumulated in equal annual instalments over the life of the unit, sufficient to equal its cost at date of retirement. As this method would result in a reserve being provided on a straight-line basis for all property classed as depreciable, assets would have been withheld from distribution as dividends which, when the business became fully developed, would approximate one-half of the difference between the original cost and the salvage value of the property. The actual retirement losses after the business had "reached its gait" would approximate the current credits to the reserve, so that the reserve accrued during the years before retirements were realized would be carried forward with no possibility of its being used to meet completed losses until the property in its entirety ceased to function.

Adherents of the second view, if entirely logical in their position, look upon the utility business as one not expected to terminate and, therefore, as one in which there will never be occasion to use the reserve accumulated in early years, to meet a realized and completed loss. They contend that because of this there is no need of providing a reserve on such basis and that all that is needed is a balancing reserve to meet actual retirement losses when and as they occur. They take the position that provision of the reserve which, according to their view, will never be needed to meet losses, is merely a means of securing capital from the customers.

Deduction of Depreciation Reserves from Rate Base

Regardless of the ultimate usefulness of such reserves to meet completed losses —which turns upon theories of actual value and expectancies as to the permanence of the utility business—there can be no question that a reserve built up on a straight-line basis serves the purpose of providing capital for the business without actual interest or dividend disbursements.

The use of an undepreciated rate base, then, in connection with a charge to operating expenses sufficient to provide a reserve on a straight-line basis, would mean that a return would be allowed to investors not only on investment represented by securities and surplus, but also upon funds furnished by customers to be used when retirements actually occur, and which, in the meantime, serve the purpose of general capital of the enterprise. A deduction for accrued depreciation seems entirely logical in such circumstances.

No Deduction of Retirement Reserve from Rate Base

Where the reserve provided is only enough to absorb retirement losses as they occur, the total credit balance will usually be relatively small. Some advocates of the "retirement-reserve" theory

go as far as to say that temporary debit balances are of no significance, that the only purpose of carrying the reserve account is to furnish a means of distributing retirement losses over a period of years, and that, in fact, no real reserve need be provided. It is their position that the so-called retirement reserve is only a vehicle for distributing losses and that the existence of a credit balance is more or less fortuitous and not an indication that a reinvested reserve has supplied a part of fixed capital.

In the recent cases wherein the lower federal courts have refused to make a deduction from the undepreciated totals, in arriving at a rate base, such reserves as have been provided to meet property losses appear to have been accumulated on the retirement principle, and not to have served to relieve the companies from furnishing all of the capital needed for construction work by means of the sale of securities or the investment of surplus earnings. Little or none of the capital, under such circumstances, would have been furnished by customers through the payment of rates. All of the capital is entitled to earnings and, if earnings are denied, the sources of capital will be dried up. Where the reserve that has been provided is a "retirement" rather than a "depreciation" reserve, a deduction for accrued depreciation does not seem fair.

If the straight-line method of providing for depreciation is contrasted with the theory that losses of value occur only as retirements are made, we find in the use of the former a logical reason for reducing the rate base on account of accrued depreciation and in the acceptance of the latter equally cogent reasons for not doing so. The reasoning supporting these conclusions, however, has not been generally applied by the courts and only in part by commissions.

The Sinking-Fund Method

Some, at least, of the state commissions which have not subscribed to the full "retirement" program have nevertheless been accustomed to make no direct deduction from the rate base on account of depreciation. In other words, the gross amount of capital is considered to be entitled to a return, even though part has been secured from rates for service. Out of this total return a portion must then be credited to the depreciation reserve which is accumulated under what is known as the sinking-fund method. The undepreciated rate base is properly used in connection with this sinking-fund method of building the depreciation reserve.

Earnings are permitted on undepreciated capital. Part of this capital, which is measurable, under normal conditions, by the credit balance of the reserve account, has been furnished by customers to provide against losses that are not complete until property is retired. If earnings are permitted on the undepreciated whole, a part of those earnings should be used to build up the reserve. To the extent that such provision is made, the amount that must be set aside as a charge to operating expenses is reduced. Through such reduction the customer is virtually paid interest for the use of reserve capital supplied by him through his payments for service. Security holders receive returns on their investments only, which is what they would receive if the rate base itself were reduced on account of depreciation. The use of an undepreciated rate base and a sinking-fund provision for depreciation is really, therefore, a means of giving effect to accrued depreciation in the rate base.

To the public service commission using this method, the problem is one of

the mechanics of rate regulation rather than one of economics. The result to the investor and to the public, over the life of the property, is the same as that accomplished by the use of a depreciated base and a straight-line provision.

Significance of Undepreciated Investment Standard

Original cost may not be value. It may not even be the most important indication of value. There may be a distinction between value and such rate base as will adequately compensate and attract capital. In practical rate regulation, original cost seems to offer assurance of stability, of comparatively cheap capital, and of adequate compensation for capital, and these factors have led to its use as a major element in the rate base, even though such base may not be identical with value.

Similarly, a rate base that is not directly depreciated may not be the value of the property; but it produces, if properly used, the same results as could be attained by direct deduction, and the convenience and ease of its use and application have led to its adoption by several commissions.

It is not fair to draw the conclusion from this that those commissions take the position that there is no depreciation in a public utility property. The sound conclusion, where the provision for depreciation is placed upon a sinking-fund basis, is that the commissions did conclude that there was an accrued depreciation, and that the convenient method of recognizing the fact was by requiring a part of the return on the undepreciated rate base to be credited to the reserve.

In some instances commissions have reduced the rate base on account of the depreciated condition of the property and have allowed as an operating expense only such charge for depreciation as would be sufficient on a sinking-fund basis. The effect of this procedure, if fully applied, is to permit the business to earn a return only on capital represented by securities and by surplus. Out of this return there would have to be credited to the reserve the equivalent of interest, in order that an adequate reserve might be accumulated. As a result, the security holder would not be in a position to take for his own a full return upon his actual investment. If a sinking-fund basis of providing the reserve is to be used, there is no warrant for direct depreciation of the rate base.

The adherence of public service commissions to original cost has been based upon what appeared to them to be sound public policy, even though it might not be complete acceptance of the law of valuations. The use of an undepreciated rate base has been a convenient way, when coupled with the sinking-fund method, of building up the reserve, of recognizing the existence of accrued depreciation. It has not constituted a denial that public utility property is subject to the effect of depreciation.

EDITORIAL NOTE: Mr. Mathew's article is the first of a series dealing with various aspects of public utility valuation problems from different points of view.

THE REAL ESTATE CODE OF ETHICS

By HERBERT U. NELSON

THE common law in English-speaking countries, which relates to business and industries, is largely an expression of trade customs of past centuries. These customs were crystallized into law several generations ago. The growth of the modern economic structure has been so rapid, and its diversification so tremendous, that it has far outstripped the law despite the relative flexibility of the common-law and equity courts. As a consequence, a vast number of abuses and situations for which the common law has no adequate remedy have arisen. For this reason courts of equity were early formed to supplement the common-law courts in cases where common-law principles were unjust in application to particular cases or were lacking. Although at first the two types of courts were distinct, in more recent times they have been merged, and judgments in equity or in common law are now usually rendered by the same court in the United States. But even the courts of equity, designed as they were to correct the deficiencies of the common law, have been unable to keep pace with the rapidly changing customs and practices of business.

Significance of Codes of Ethics

In this situation codes of ethics perform a function that is similar in some respects to that of early equity courts. Trade and vocational associations, brought together in the first instance by a desire to promote their own interest through exchange of experience and through common action in matters of policy, have sensed this lag of the law behind business practice. Especially in the last few years have trade associations tried to meet this situation by setting up standards of practice, or codes of ethics, to serve as guides for their own members as well as for the public. It is noteworthy that during the past 15 years more than 100 national trade and vocational organizations, not to mention many regional or local associations, have adopted such standards of practice.

It is significant that such standards are often called codes of ethics. This nomenclature is a recognition of the fact that there is a moral content in the inhibitions which any trade association sets up for its members. It is a recognition of the fact that any trade or vocation has a responsibility to society as a whole for the activities of its members. It is an admission that the ordinary acts of business have repercussions in the social structure for which business men must accept responsibility. It is further evidence of the growing realization that regard for the public welfare is good business practice.

The essential feature of a code of ethics is that it embodies the business as well as moral judgments of the group of men who actually furnish a service. It is not superimposed from without, but springs from within, a business or profession. Implied in these codes is a separation of the good from the bad practices and a formulation of the socially good practices as a standard of conduct for all members of the business group. At the heart of a well-considered code of ethics is the idea of public service—that the best practices from the public point of view are also the best

practices from the private point of view.

The codes of ethics which have been prepared during the past 15 years cover almost the entire range of American business. The academician may note with some amusement that the ice-cream manufacturers or the icemen have a code of ethics. The fact that they and so many other types of business do have such codes, however, is one of the most significant phenomena of current times. It is many times more significant with regard to the future of our society and our business structure than the political news which holds the center of the stage. It means that American business is developing a social conscience. American business is admitting that individualism must be tempered with due regard for the general welfare, that the purpose of business activity is not profit solely, but a service to society.

Adoption of the Real Estate Code

Among the first codes of ethics to be adopted was that of the National Association of Real Estate Boards. Previous to that time (1908) only three other codes had been adopted in this country. These were the codes of the United Typothetae, medicine, and law.

When the Real Estate Code of Ethics was first promulgated, there were many debates concerning its advisability. Many men in the real estate business felt that the very adoption of such a code carried the unfavorable implication that men were guilty of practices which necessitated such action. Many members felt that it was no part of the duty of a trade association to attempt to govern the business conduct of its membership. All that was needed, they said, was a sincere willingness to deal fairly with every one. If a man were actuated by such motives, he needed no specific guides.

Opponents of this point of view retorted that a code was necessary because, although all the members might desire to do the right thing, they could not always agree on what the right thing was. It was pointed out that the average man in the real estate business, as well as in other lines of business, did try to deal fairly with every one. The man who was guilty of deliberate wrongdoing was probably exceptional and would not, in any event, be bound by regulations voluntarily assumed. However, in a given typical situation where personal interests were involved, responsible men would have honest differences of opinion as to the correct course of conduct. In view of this difficulty, therefore, it was deemed necessary that the lessons of experience should be assembled and formulated, and that the collective conscience of the entire vocation should speak its mind with regard to the right course of conduct in the typical situations which daily confront the real estate man.

The code was adopted. It was sent broadcast throughout the country and was read with interest by real estate men and by the public. There were, however, no sanctions behind the code, except that of the force of opinion. Nevertheless, the code established criteria by which conduct in the real estate business came to be judged both by the public and by those practicing the business. This process went on for 15 years until, by a process of reiteration and education on the part of the leading men in the association, the code was more or less taken for granted.

Enforcement of the Code

A year ago, at the annual convention

of the national association in Washington, the committee on ethics presented a revised code which formulated still more clearly and definitely the obligations of the real estate man in a given situation. The revised code was accepted without debate, and this convention went much further. It approved a by-law which made obligatory the adoption of the code by all the 516 boards constituting the national association, and imposed upon these boards the duty of rigidly enforcing the code against all members in their respective jurisdictions. Any board which neglected to enforce the code might be expelled from the association. This by-law placed behind the code a stronger moral sanction than had previously prevailed.

We are aware that sceptics have sometimes questioned the efficacy of this code on the ground that the sanction is a mere paper sanction that is never enforced. But it should not be forgotten that the mere existence of the code, adopted and supported by leading successful real estate men in a community, constitutes a check upon the conduct of those who might be disposed to overstep the line. In almost any business, men hesitate to incur the moral disfavor of their business associates. Moreover, instances are recorded where disciplinary enforcement has been applied. I have in mind a recent case of a real estate dealer who misrepresented to a prospective house purchaser the quality and condition of a furnace. The dealer was suspended from the board. And although the national association has not yet had occasion to suspend a member board for not living up to the code, there is no reason to suppose that the association would not take this step if the situation required. The acceptance of a law cannot be adequately gaged by the discipline of its breaches.

On the other hand, there is ample evidence that the code today is taken seriously. It is an active guide to business policy. It is, on the whole, as carefully observed as though it were written into the statutes.

Scope of the Real Estate Code

The realtor's Code of Ethics today is divided into four parts. The first part has to do with professional relations. It sets forth the duty of the realtor to share the lessons of his experience with others through his organization, the real estate board; his obligation to settle controversies with other realtors by arbitration; to submit to the officers of his board all pertinent facts when he is charged with unethical practice; to avoid criticism of a competitor; to let a competitor's transactions alone; to respect his competitor's clientele.

The second part of the code sets forth the realtor's duties to his clients. As a rule, a real estate man is, under the general law of agency, the legal representative of the owner. He is directed, however, to be fair to a purchaser or tenant, although his primary obligation is to his client. He is forbidden to buy for himself property entrusted to him for sale, without first making his position clearly known to his client. He is forbidden to give offhand opinions as to values, and is directed to render such opinions only after having collected the necessary data and formulated them into a reasoned judgment. He is forbidden to accept commission, rebate, or profit on expenditures made for the owner without the owner's full knowledge and consent. He is directed to have a written contract with his client, setting forth clearly the obligations of each party, so as to eliminate the errors and misunderstandings that arise from

purely verbal agreements. He is directed not to enter into an exclusive contract to sell property for an owner unless he is prepared to render an adequate service. He is directed to render appraisal services in a professional manner, regardless of expediency or instructions from clients that might tend to warp his judgment.

As an illustration of how rules of conduct among business men creep into the established law, the case of *Maxwell* v. *Massachusetts Title Insurance Company,* 206 Mass. 197 (1910), may be cited. The main point at issue was a real estate broker's right to act as an agent and a purchaser for his own account at one and the same time. On that point the court said, citing a principle which is derived from early principles of equity in agency cases:

> A broker cannot purchase for his own use the property entrusted to him to sell. His fiduciary obligation requires him to procure the highest price obtainable, while his personal interest as a buyer is directly antagonistic to that of his principal. The attempt of a broker thus to serve two masters is a fraud upon his employer, and is against public policy, and deprives him of any right to a commission.

This principle, as the court said in an earlier case, is not only well-settled in law, but is "common business morality." Although this rule is old in legal history, its appearance in the law shows how equity courts took over the moral standards of business men.

The Public Relations of Realtors

The third part of the code constitutes a new element in such documents. It sets forth the relationship of the real estate man to his customers and to the public. As a rule, most business codes have dealt almost exclusively with intertrade or interprofessional relationships. The realtor's code, however, recognizes that the good transaction is the one which benefits all parties concerned in it, and that it is the obligation of the realtor not only to serve his client, the owner, but also to serve and have due regard for the interests of the buyer and the public. In this part of the code, therefore, the realtor is directed to protect buyers and the public against fraud and misrepresentation; to offer property solely on its merits without any exaggeration or misleading representation; to have in hand exact data concerning all property offered, so that he may inform buyers and the public accurately. He is forbidden to offer property at a price higher than that which the owner has openly agreed to take. If he has an ownership interest in any property which he offers for sale, he must disclose such interest to all parties to the transaction; otherwise it is clear that his function as a middleman could not be disinterested. He is directed to inform the purchaser that he is acting in the seller's interest, so that the purchaser may have this fact in mind and properly safeguard his interests. He is forbidden to accept compensation from more than one party to a transaction without the full knowledge and consent of all. He is prohibited from permitting any property in his charge to be used for illegal or immoral purposes. He is instructed to advise the use of legal counsel whenever the interests of any party to a transaction would seem to require it. He is directed to inform all parties fully and in detail as to his own charges whenever an agreement to a transaction is arrived at, so as to avoid later misunderstanding. He is directed to have all contracts and agreements in writing. He is forbidden to introduce into any neighborhood a character of occupancy

or of property, the members of any race or nationality, or any individuals whose presence will be detrimental to the neighborhood and to its property values. No instructions from a client can in any degree abrogate the realtor's obligation to the code.

The fourth part of the code consists of suggestions to the public. It is recognized that the public is not subject to regulation. If the general public, however, in its dealings with real estate men will respect the standards of practice which they have themselves set up, every one can act on certain common understandings and every one will benefit. The public, therefore, is urged, when dealing with a broker, to consider the relationship a confidential one and not to quote to others the terms and properties which a broker offers. It is suggested that by selecting a single experienced broker and dealing exclusively with him, one will obtain better service in the long run. It is suggested also that no one should offer his property for sale unless he is ready and willing to sell it at the price quoted. Many persons offer property for sale only in order that they may gain some knowledge of its market value, and have no intention of consummating a transaction. Naturally such action leads to difficulties. Owners of property are urged to assume the same attitude toward a realtor's judgment with respect to property as they would toward the expert opinion of a doctor or lawyer.

A Declaration of Faith

In the preface to the code occur the following statements:

> Under all is the land. Upon its wise utilization and widely allocated ownership depend the survival and growth of free institutions and of our civilization. The realtor is the instrumentality through which the land resource of the nation reaches its highest use and through which land ownership attains its widest distribution. He is a creator of homes, a builder of cities, a developer of industries and productive farms.
>
> Such functions impose obligations beyond those of ordinary commerce; they impose grave social responsibility and a patriotic duty to which the realtor should dedicate himself, and for which he should be diligent in preparing himself. The realtor, therefore, is zealous to maintain and improve the standards of his calling and shares with his fellow realtors a common responsibility for its integrity and honor.

This constitutes the realtor's declaration of faith. It recognizes his economic function and recognizes also the fact that any one who performs an important economic function also has an important social responsibility.

In the course of this article, the term "realtor" has been used frequently. This term was coined by Charles N. Chadbourn, of Minneapolis, and was adopted by the national association in 1917 as a membership designation. It is the exclusive property of the association, and the national association's legal title to it has been upheld in several instances. By adopting this designation, the real estate man has attempted to express the ideals for which he stands. By the very act of calling himself a realtor, he announces to the public that he is bound, in his business activities, to observe the standards which his national organization has established. The use of the term "realtor," therefore, is in itself a profession of adherence to the code.

License Laws Differ from Code

Emphasis should be given to the fact that the coinage of the term "realtor" and the formulation of the above Code

of Ethics are part of a spontaneous movement within the real estate business itself. These standards of conduct are not imposed from without by governmental authority. Hence, the Code of Ethics should not be confused with the real estate license laws which have been enacted in almost a score of states. These laws, it is true, lay down certain standards which must be lived up to under penalty of a revocation of the license by state authority. But such laws apply to prospective entrants into the real estate business and are designed to protect the general public from the fraudulent practices of that fringe of unscrupulous business men that surrounds even such well-established professions as the law or medicine. In short, license laws and the Code of Ethics cannot be identified—the one is imposed by external governmental authority and is limited in scope and purpose; the other is voluntary, spontaneous, broad in scope, and designed to raise the plane of real estate practice above any legal level fixed by statute or by court decision.

Education and the Code of Ethics

The realtor goes even further than a codification of standards of conduct; he is setting about the task of educating himself up to and beyond the obligations of the code. In other words, the realtor recognizes that a proper fulfilment of his social obligation depends not only upon the observance of certain standards of business practice, but also upon more efficient conduct of his business for which study and education are necessary. He has, therefore, undertaken an organized program of real estate education, which in its rapid progress has outstripped all similar efforts. In a brief period of 18 months an educational program has been organized on a national scale and has been installed in more than 170 cities, including 33 universities. Professor Richard T. Ely has described this work as "one of the greatest movements in education and research of the present century. The National Association of Real Estate Boards through its educational program and its Code of Ethics for its members has made greater progress toward the status of a profession than has any other business or profession in an equal period of time."

Real estate education bears a very definite relation to the Code of Ethics. In that connection the realtor's course of study may be said to have a threefold function: (1) It reveals more clearly the meaning, practical advantages, and social importance of the code; (2) it helps to educate the conscience through the education of the head; and (3) it so quickens the perception of right and wrong conduct that it tends to supplement enforcement proceedings by making them unnecessary. In adopting such a program of study realtors have given application to the principle that ethical service is intelligent service. And this principle is implicit throughout the Code of Ethics.

Already this educational work is having a profound influence on the realtor's conception of his business. It is bringing him in contact with cultural and social considerations which are modifying his activities in many important respects. The results will in a few years be evident to every one not only in the manner in which the business is conducted, but in the more concrete form of more livable and beautiful cities and communities. For the realtor is, above all, a community builder.

THE UNIFORM ACCOUNTING SYSTEMS ADVOCATED BY UTILITIES COMMISSIONERS

By HIRAM T. SCOVILL

DURING the last decade there has been a marked tendency toward consolidation of public utilities. Such consolidation results, in many cases, in combining utilities from several states. This type of affiliation has gradually caused sentiment in favor of a more uniform method of accounting for the utilities throughout the United States. The movement in this respect might be compared with that which fostered the Uniform Negotiable Instruments Act, the Uniform Sales Act, and others.

The advantages of a uniform accounting system for each type of utility throughout the United States had been recognized for several years, but not until 1919 was definite action taken toward the establishment of such uniformity. At the annual convention of the National Association of Railway and Utilities Commissioners held in Indianapolis in 1919, the Committee on Statistics and Accounts of Public Utilities was authorized to formulate and present to the individual state commissions uniform accounting systems for public utilities other than railways. The national association received the report of the committee at the next convention, held in Washington, D. C., on November 12, 1920. The report consisted of the complete system of accounts for gas utilities and for electric utilities, but not for others. They were to be prepared later.

The convention then adopted resolutions as follows:

"Resolved, (1), that the report of the Committee on Statistics and Accounts of Public Utilities be received and printed.

"2. That this convention recommend that member commissions give careful consideration to the proposed uniform system of classification of accounts for electric and gas companies and adopt them, unless they are found to conflict with local statutes, with such modifications as may be necessary to meet local conditions.

"3. That this convention recommend that, wherever practicable, the calendar year be made the fiscal and reporting year.

"4. That this convention recommend to all state commissions which adopt the standard classifications of accounts proposed by this committee, that questions of interpretation be referred to the Standing Committee on Statistics and Accounts of Public Utilities for an expression of opinion, acting in cooperation with the accounting sections of the National Electric Light Association and American Gas Association."

I. Scope of Uniform Accounting Systems

Since that time many other states have adopted uniform systems substantially as prepared by the committee in 1920, which consisted of O. O. Calderhead, of Washington; W. M. Hammond, Illinois; George C. Mathews, Wisconsin; H. C. Hasbrouck, New York, second district; Harry Boggs, Indiana; and C. J. Green, Oregon.

In addition to the uniform systems for electric and gas utilities presented and approved in 1920, the association has approved a system for water companies. As yet, systems for other local utilities have not been adopted by the association.

According to a memorandum from the National Electric Light Association dated March 1, 1925, 25 states have adopted the uniform accounting system for electric utilities. The same states have, practically without exception, adopted the system for gas utilities. They are: Alabama, Arizona, Arkansas, Colorado, Connecticut, Georgia, Idaho, Illinois, Indiana, Kansas, Massachusetts, Maine, Michigan, Nevada, New Jersey, New York, North Dakota, Tennessee, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, Wyoming.

In addition to these, the Public Service Commission of Oregon has adopted the system for electric companies (and, presumably, for gas companies), beginning January 1, 1925, according to an excerpt from *Electric World* for January 24, 1925.

Of the states mentioned as having adopted the uniform classification for electric utilities, Massachusetts, Maine, and New York have adopted it with slight modifications, in order to comply with some of the state laws.

The same memorandum of the national association referred to above shows that 13 states have not adopted the uniform classification, namely: District of Columbia, Louisiana, Maryland, Missouri, Montana, New Hampshire, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, and South Dakota. Of these states, North Carolina has issued a form of annual report based on the classification of the National Association of Railway and Utilities Commissioners, and will very likely follow it with a classification of accounts. It has had no classification heretofore. Although Maryland has not adopted the classification of the national association, its commission has issued an order allowing two of the largest companies in Maryland to use it. Of the 11 other states not mentioned above, one, Delaware, has no utilities commission, California has adopted the classification of the Federal Power Commission, and 9 are not under the jurisdiction of the commissions with respect to accounts of electric companies. These 9 are: Florida, Iowa, Kentucky, Minnesota, Mississippi, Nebraska, New Mexico, South Carolina, and Texas. In the states in which the commissioners have no jurisdiction over the accounting of utilities, most of the larger electric companies (at least) are following the classification adopted by the National Association of Railway and Utilities Commissioners.

It is interesting to note that with excellent progress toward general uniformity in classification of accounts, a movement is under way to establish uniform annual reports. The national association, at its 1924 convention, held in Phoenix, Arizona, adopted a standard form of annual report for electric and gas companies and recommended the same for adoption by the several states. At this same convention, a simplified classification for use of the small Class C and Class D electric utilities was also adopted.

Liberal Features of the System

The adoption, by any state, of the uniform systems recommended by the association does not mean that the utilities of that state must completely revolutionize their accounting procedures,

nor does it mean that the state commission must make radical changes in its existing uniform systems. In fact, most states had systems in force which were practically the same in general principles as the uniform systems now being considered. There were, however, some terms and principles in accounts and some features of the financial statements which differed materially in the systems of the several states. These differences were reconciled, if not compromised, in the systems of the association.

The accounting systems recommended by the association follow the generally accepted procedures and forms of industrial and commercial enterprises in many respects. The original purpose of the accounting system as an aid to regulation, however, is not overlooked in the provisions incorporated into the systems. Accordingly, some features are included which would not appear in a uniform system adopted by a trade organization. The accounting system or device that assists in regulation must naturally be more specific and "hidebound" than one adopted by a group of executives voluntarily for the purpose of comparing results one with another.

The authors of the uniform systems suggested by the National Association of Railway and Public Utility Commissioners cannot be given credit for building a new structure from the ground up. They have, however, refrained from making revolutionary changes in the existing systems. They have been temperate and conservative. The systems of the Interstate Commerce Commission and of the better state utilities have been used to a large extent in the preparation of the systems finally approved by the association. The task of modifying, however, even to the slightest extent an existing system of accounts and the descriptive classification thereof is a very exacting one because of the intricate interdependence of items throughout the manual. A change in one principle might require a score or more of changes in the descriptive material in the printed system of accounts. For this reason, and for the excellent correlation which was finally established among all phases of the system, the authors deserve a deal of credit. They showed their intimate knowledge of public utility affairs. They displayed a keen appreciation of the accounting problems that come before the accountants of the utilities and of the commissions, and, best of all, they seemed to be able to anticipate many of the questions that would arise in the operation of, and in regulation through, the system.

A flexibility is provided for, in many places, in the descriptive matter affecting accounts. Utilities are not bound to do things in one way and no other. There is, of course, the usual provision that utilities of smaller productive capacity, as gaged by operating earnings, need not use all of the accounts that larger utilities do. There are four classes of utilities provided for in the gas and electric utilities, as follows: Class A—Corporations having average annual operating revenues exceeding $250,000; Class B—Corporations having average annual operating revenues exceeding $50,000, but not over $250,000; Class C—Corporations having average annual operating revenues exceeding $10,000, but not over $50,000; Class D—Corporations having average annual operating revenues of $10,000 or less.

In many places throughout the description of the accounts, it is evident that utilities even of the same type and class have the opportunity of exercising

considerable initiative with respect to the methods of keeping their accounts. Some of these are presented later in this article.

The Numbering System

By a unique numbering system the accounts prescribed for utilities of each class are clearly designated. It is among the expense accounts only that any distinction is made between one class of utility and another. In the asset, liability, and income accounts, there is little, if any, opportunity for the commission to offer an option of account titles if it expects to have fundamental information presented through the accounts.

The method of relieving the smaller companies from keeping the numerous expense accounts required of the larger ones may be illustrated by quoting from the *Uniform System of Accounts for Electrical Corporations.* One of the main divisions of expense is called "distribution expenses." In the classification the accounts to be kept under this heading are shown as follows:

			740	DISTRIBUTION EXPENSES
D			741	Distribution operation and maintenance
C	B	A	741.1	Distribution superintendence
C	B		741.2	Distribution supplies and expenses
		A	741.21	Distribution maps and records
		A	741.22	Distribution office expenses
		A	741.23	Distribution miscellaneous expenses
C	B		741.3	Operation of distribution lines
		A	741.31	Labor and expense—subways
		A	741.32	Labor and expense—overhead conductors
		A	741.33	Labor and expense—underground conductors
		A	741.34	Labor and expense—telephone system
C	B		741.4	Meter operation
		A	741.41	Salaries and personal expenses, meter department
		A	741.42	Testing meters
		A	741.43	Miscellaneous expenses, meter department
		A	741.44	Removing and resetting meters
		A	741.45	Removing and resetting transformers
C	B	A	741.5	Maintenance of underground conduits
C	B		741.6	Maintenance of lines
		A	741.61	Maintenance of overhead conductors
		A	741.62	Maintenance of poles, towers, and fixtures
		A	741.63	Maintenance of underground conductors
C	B	A	741.7	Maintenance of services
C			741.8	Maintenance of transformers and meters
	B	A	741.81	Maintenance of line transformers
	B	A	741.82	Maintenance of consumers' meters
C	B	A	741.9	Maintenance of buildings and grounds

The tabulation above means that all distribution expenses bear numbers between 740 and 750. It seems, further, that there is only one main subtitle under "distribution expenses," and it is designated as "741—Distribution operation and maintenance." Furthermore, this is the only account the small Class D companies are required to keep to record details of distribution expenses. This is learned by observing that the letter "D" does not appear before any other account title under "distribution expenses." By a similar scrutiny of the letters placed before the account numbers it is seen that Class A companies are required to keep all of the accounts shown in the list above, except those six which are reserved exclusively for the smaller companies to use in place of several more minutely classified accounts.

In this specific group, called distribu-

tion expenses, it seems that the Class B and Class C companies are required to keep the same accounts except under maintenance of transformers and meters, where Class C companies may keep just the one account designated as 741.8, while Class B companies are required to keep two, designated, respectively, as 741.81, maintenance of line transformers, and 741.82, maintenance of consumers' meters.

A similar distinction between Class A companies and Class B, C, and D companies is made in the other types of expenses. It should be observed in this connection that a company of a given class may use accounts prescribed for a larger company if it chooses, but it may not use those prescribed for a smaller company. For example, a Class D company may use accounts prescribed for a Class A, B, or C company, and a Class B company may use those prescribed for a Class A company, but a Class B company may not use those prescribed for a Class D or C company, except as specifically provided for in the classification.

The account numbers used in the distribution expenses above represent the Dewey decimal system, which is used throughout the uniform systems of the National Association of Railway and Public Utilities Commissioners. In the general instructions, however, the authors say: "The numbers prefixed to acccount titles in this classification are solely for convenience of reference and are not part of the titles or definitions."

There are several types of numbering systems for accounts in industrial and public utility accounting, but the type used in the systems of the railway and utilities commissioners is the one generally recognized as superior to the others. The general plan of this system is presented here in outline form:

ASSET ACCOUNTS

101 Fixed capital
- 301-310 Intangible fixed capital
- 311 and subdivisions Land
- 312 and subdivisions Structures
- 313-327 and subdivisions Equipment
- 328 Miscellaneous tangible equipment
- 351-359 Overhead costs during construction

111-119 Current assets
121-129 Miscellaneous assets, including Funds
131-139 Suspense
141-149 Adjustment accounts
150 Profit and Loss—deficit

LIABILITY ACCOUNTS

201-209 Capital stock and similar accounts
211-219 Long-time debts
221-229 Current liabilities
231-239 Accrued liabilities
241-249 Advances from affiliated companies, etc.
251-259 Reserves
261-269 Miscellaneous unadjusted credits
270 Profit and Loss—surplus

INCOME ACCOUNTS

401 Operating revenues
- 601-609 Sales of current (or gas or water)
- 611-619 Miscellaneous revenues

402 Operating expenses
- 701-709 Production expenses
- 710-719 Purchased current (or gas or water) and residuals and gas generation for electric utilities
- 720-749 Conversion, transmission, and distribution expenses
- 750-759 Utilization expenses
- 760-769 Commercial expenses
- 770-779 New business expenses
- 780-790 General and miscellaneous expenses

403 Uncollectible bills
404 Taxes
410-419 Net income from leased properties
421-429 Net income from non-operating properties
431-439 Financial expenses
441-449 Appropriations of net income

Some Technical Features

The state utilities commissions, in one sense, occupy a position with respect to local utilities similar to that of the Internal Revenue Department of the Federal Government with respect to income tax payers of the country. They must require a good accounting procedure based on correct accounting principles, but flexible enough to permit of

obtaining the same net results under methods best suited to the respective business concerns. At the same time, they must inject enough provisions to permit the commission to control certain actions of the utilities in accordance with the best public policy.

If accounting procedures were well enough standardized, or even if accounting employees knew enough about usual procedures, both the utilities commissions and the Internal Revenue Department could quote their instructions in words similar to these: "To the utilities (or taxpayers): Keep your accounts in accordance with the generally accepted accounting procedure, except that the following provisions must be observed to assist in the administration of the laws and to meet the demands of public policy." Then would follow probably 10 or 20 brief paragraphs dealing with the exceptions. Since the science of accounting has not reached such a plane, and since all accounting employees have not learned adequately even the principles of accounting that are generally recognized as correct, both the utilities commissions and the Internal Revenue Department find it necessary to issue elaborate pamphlets and supplementary instructions concerning the keeping of accounts and the preparation of reports.

For this reason, the uniform system of accounts of the railway and public utilities commission is composed largely of instructions which tell the bookkeepers what good accounting principles are in their respective fields. In some cases, it is necessary to describe the keeping of accounts in a specific way, since accountants differ as to theories to be applied. In such instances, the commission deems it best to take a specific stand for one theory or another. In other cases, the commission permits the utility to exercise an option in using one method or another. This makes the system flexible, and is a very desirable feature from the point of view of the utility.

II. Some Debatable Features of the Uniform System

We shall present, first, some of the debatable procedures in accounting on which the uniform system under discussion takes a definite stand on one side or the other; and then we shall present some of the prominent instances in which the system permits the utility to exercise an option in the keeping of some of its accounts. Points in accounting theory which are debatable and on which the authors of the uniform system have prescribed a definite procedure are as follows:

Funds. The system says that "Funds are assets . . . ." It is sometimes contended, though not by the best accountants, that funds are the same as reserves. It is well that the authors covered this item specifically.

Retirement reserve. One of the most interesting departures from ordinary terminology found in the uniform system is the use of the term "retirement reserve" for "depreciation reserve," and of "retirement expense" for "depreciation expense" or "depreciation." There is no option on this point and the authors feature this by providing that, "If the accounting company has, previous to the effective date of this uniform classification of accounts, maintained a reserve under some other title, such as 'depreciation reserve' for the purpose of equalizing retirement losses, the balance in such reserve, as at the effective date of this classification, shall be transferred to this account."

The adoption of the word "retirement" instead of "depreciation" in both the reserve and the expense account seemed of sufficient importance to the subcommittee of the National Association of Railway and Utilities Commissioners to cause it to comment specifically thereon in its letter of transmittal of the system as follows:

> The National Association Committee has recognized the importance of uniform terminology and at the Chicago conference, in April, the constant endeavor was to select terms and definitions which would be as free from ambiguity as possible. It was with this thought in mind that after a prolonged discussion the National Association Committee decided to discard altogether the word "depreciation" and to accept the substitute term proposed by the National Electric Light Association and American Gas Association accountants, "retirement expense." It was felt by all that "depreciation had come to have so many unfortunate connotations, that clearness and uniformity of interpretation could best be attained by using an entirely different term.

A few rather unusual features are provided for the operation of the retirement-reserve and retirement-expense accounts which are, nevertheless, capable of being supported by logical business expediency. On the other hand, a slight ambiguity is found in one or two of the comments on these accounts. One good feature is that the retirement-reserve account is looked upon as one to provide for replacement of full units of property when they become obsolete or are abandoned for any other reason. In this sense the reserve is not a valuation account and it is not so treated. It is to be credited, and retirement expense charged, with amounts periodically "in addition to the necessary cost of keeping the plant and equipment in a high state of efficiency through charges to the regular maintenance accounts." Furthermore, it is stated that "the losses which this account is intended to cover are those incident to important retirements of buildings, of large sections of continuous structures like gas mains (or electric line), or of definitely identifiable units of plant or equipment, and the object of the account is that the burden of such losses may be as nearly as is practicable equalized from year to year."

With this specific description of the account placed before the utilities, it is apparent that they are expected to have rates to consumers set high enough to permit them to keep all units of fixed property in excellent repair, and also to provide for retaining in the business a sufficient amount of assets to finance the replacement of any substantial amount of fixed property from time to time as conditions seem to demand. A retirement fund for all or any part of the reserve is optional.

A further invitation is extended to the utilities to charge all that is necessary against the cost of operation for such anticipated retirement, in these words:

> Note: It is the intent of the classification that a reserve shall be provided sufficient to cover all retirement losses that may reasonably be expected. If the accounting company does not do this, and, later, finds that retirement losses are incurred in excess of the amount that has been provided, the charging of such losses to operating expenses either directly or through the suspense account "property abandoned" does not bind the regulatory commission to the acceptance of such charges as part of the necessary current cost of maintenance.

The essence of this quotation might be interpreted as a warning to the utility to charge against earnings, each year, all that its officers can imagine should be necessary to build up a retirement reserve, because, if it does not do so, it might not later be given relief

by the commission for losses or retirements not so anticipated and provided for.

Depreciation or retirement expense in connection with property has a two-fold effect on the financial statements of a business—it tends to reduce the balance-sheet value of the assets and to increase the costs of operation (decreasing profits). In these times, when courts and commissions are ruling in favor of the present replacement cost (less depreciation) as a basis on which to calculate a fair return to a utility, it would seem that any effect of depreciation entries on the balance-sheet is of little importance. The effect on the income statement, however, is of considerable importance. It permits the utility, theoretically, to obtain rates which will enable it to pay ordinary dividends and preserve enough in the business to replace, to any reasonable extent, properties retired for any reason. If a utility should build up its retirement reserve as rapidly as it seems to be invited to do by the wording of the note quoted above, it would be quite sure to have a reserve equal to the balance of the asset account long before the asset was ready for retirement. The result would be that the balance-sheet value of the asset would approach zero while it had an operating efficiency and probably a sale value of 80% of original cost. It is this possible situation which probably causes the authors of the system to provide that retirement reserves shall be shown among general reserves on the liability side of the balance-sheet, instead of being shown as deductions from the fixed assets.

Some misunderstanding is likely to arise from the use of the phrase "ledger value" in connection with retirements. It is defined as "the amount originally charged" in the paragraph on "withdrawals and retirements" under the "general instructions and definitions of fixed capital accounts." In notes A, B, and C, under the description of account number 251, "retirement reserve," the following provisions are made:

Note A: When property is retired whose *ledger value* has been reduced below original cost, only the remaining *ledger value* shall be written off as retirement loss.

Note B: When any property is retired whose *ledger value* is greater than the known or estimated cost, such excess shall be charged to profit and loss.

Note C: If any property is sold for more than its original cost, the excess of its selling price over *the cost* of the property plus the cost of dismantling and selling, shall be credited to this account.

The rules stated in Notes A and B seem reasonable under the ordinary interpretation of the term "ledger value" but not under the definition referred to above as "the amount originally charged." "Ledger value" is usually thought of as the asset balance minus the balance of the reserve account applicable thereto. Note C does not seem reasonable unless "the cost of the property" is changed to read "the ledger value of the property" signifying asset minus reserve valuation. If Note C is applied as printed, it means that the retirement reserve account is increased by the sale. Assume, for example, a property with a cost of $100,000, including dismantling and selling, against which a reserve of $20,000 had been created at the time of its sale for $110,000. The entry for the sale in accordance with the instructions in Note C would be:

Dr. Cash	$110,000	
Cr. Property ...		$100,000
Cr. Reserve for Retirement		20,000

This would close the property account and leave the reserve account with a

credit balance of $30,000. What would this balance in retirement reserve account mean after the property against which it was created had been sold? It would mean that it would be treated as a deferred income to subsequent operations, because for several periods retirement entries could and should be made less for the then existing properties in view of the reserve already set up. An account which thus reduces the periodical charges against operation, increases the profits and, hence, acts as a deferred credit to income. If that is what the commission considers it, then it would seem best to call it that and describe the procedure for a sale of property above cost accordingly. This would still not remove the apparent inconsistency of the use of the words "ledger value" and "cost."

Discount and premium on capital stock. The uniform system seems to imply that a utility may be given permission to distribute some of its premium on capital stock to its stockholders. It also permits the utility to reduce premium by appropriations from surplus, or by assessment levied on the stockholders. Discount on stock cannot be considered as a part of the cost of operation in any sense nor as a part of cost of construction of physical property. Premium cannot be considered as an income in any sense. Either premium or discount on stock, however, may be adjusted directly through profit and loss for the proportion of premium or discount on stock reacquired. These principles are in accord with good accounting practice and conform to Interstate Commerce Commission procedures, although they differ from the ideas of those who advocate that discount or premium on stock should remain on the books indefinitely without modification.

Discount expense and premium on long-term debt. It seems that the straight-line basis of writing off bond discount and expense, on the one hand, and premium, on the other, is required, according to the general description of the subject under balance-sheet accounts. In the description of the accounts, however, both in amortization of debt discount, and expense and amortization of premium on debt, there seems to be an intimation that the more scientific method involving the effective rate of interest is allowable. This idea is obtained from the following sentence: "This proportion" [meaning discount or premium remaining unamortized] "shall be determined according to a rule the uniform application of which, during the interval between the issue and maturity of any debt, will completely amortize or wipe out the discount at which such debt was issued and the debt expense connected therewith."

There is a well-established rule in connection with bond discount and premium that the discount or premium amortized or accumulated shall follow the interest. That is, the effective interest becomes greater than the nominal interest as discount is written off from period to period, while it becomes less than the nominal interest as premium on bonds is written off. Ordinarily, such additions or deductions from the nominal interest are merged in the interest account at the time of making the entry for the interest payment. In the uniform system under consideration, however, the actual interest paid on long-term debts is charged to the appropriate interest account. The general principle of having discount follow the interest, however, is observed in the end by bringing together the interest and the amortization accounts referred to—both debit and credit—in the same section of the

income statement designated as "deductions from gross corporate income."

Fixed capital. It seems rather unfortunate that the title "fixed capital" is used rather than "fixed assets" as a balance-sheet title. The term capital from the economic sense is permissible, but from the accounting point of view the term "capital" is likely to be confused with the term "capital stock" on the other side of the balance-sheet.

Purchase discount. No account is provided bearing a title "purchase discount" or other similar designation. It is intended, it seems, that discounts allowed the utility for prompt payment are to be deducted on the face of the invoice whenever possible, thus reducing the cost of the fixed assets acquired or of the materials and supplies put into stock. In case the utility's method of operation does not make it feasible to deduct the discount before entering the invoice on the books, such utility may credit the discount to miscellaneous construction expenditures or undistributed general expenses, according as such materials and supplies are intended for construction or for use in general operation. The results of utilities are rendered comparable, however, to a certain extent whether purchases of materials and supplies for operation are entered net or gross, because the balance of the account "undistributed general expenses" is included as a part of the costs deducted from gross operating income. If the undistributed general expense were treated as a financial expense, comparison would not be possible between utilities.

Work in progress. The uniform system provides that the cost of construction work shall be carried in several detailed progress accounts until completed, when proper allocation will be made to the several fixed-asset accounts. Some flexibility is provided, however, and the commission safeguards itself in the matter of allowing duplicate costs to stand on the books for a single unit of property in making the following provision in describing the account "work in progress":

> Charges for additions to fixed capital not involving replacements, or for improvements which necessitate retirements or reconstruction of existing property when full credits have been made in advance to fixed-capital accounts to cover the ledger cost of property retired, may be carried in fixed-capital account number 359, "unfinished construction."

Treasury securities. The use of the term "treasury securities" to designate those which have been only nominally issued rather than actually issued is very unfortunate. Accounting writers and educators have been trying, for a number of years, to have the terms "treasury stock" or "treasury bonds" applied only to such securities as have been issued and outstanding at some time, but which have been received back into the treasury of the issuing company either by gift or purchase. During the past few years all indications have pointed to the substantial adoption of that meaning in all industrial, commercial, and financial accounting. The authors of the uniform systems for utilities, however, seem to use the term "reacquired securities" for those which have been received back by gift or purchase. The term treasury securities is then used in place of "unissued securities," as they are more generally called. Thus one of the important items in a uniform accounting terminology is given a severe setback.

The main reason for using the term treasury securities for those which have never been issued seems to rest on the

idea that they have been nominally issued as a result of their having been signed, sealed, and placed with the proper officer for sale and delivery. Although this point is generally recognized as being rather an important one with respect to the liability of the issuing company on bonds, it is not so important on stocks. In either case, the term treasury stock (or bonds) should be used only for reacquired securities, and another title, probably authenticated stock (or bonds) for those securities which have been signed, sealed, and delivered to the proper officer or agent for sale. The term "authenticated" describes the conditions and relieves the term "treasury" for the more generally accepted meaning it has merited in recent years.

Interest on consumers' deposits. Amounts paid by a utility to customers as interest on meter deposits in accordance with state laws are chargeable to miscellaneous interest deductions as a main title. Of course, a utility may keep specific subsidiary accounts which can be grouped under the main title in the financial statements. If the utilities commission is to protect the people, it would seem that it should require interest on customers' deposits to be maintained and reported as a separate account. It could then determine, as it must now know from experience, that a utility does not pay interest to more than a very small group of the consumers who have meter deposits with the utility companies.

Another point in connection with interest on customers' deposits which may be criticized is its location in the income statement (or account, as it is carelessly designated in the uniform system). Customers' deposits are required on meters, in most cases, to protect the utility from bad-debt losses. Any cost of carrying these deposits, it would seem, should therefore be included in the same division of the income statement as the uncollectible bills. This latter item is included in the part of the statement in which is derived the amount of gross profit from operations, while miscellaneous interest deductions are shown as financial expenses under the heading "deductions from gross corporate income." Furthermore, this latter section of the income statement is intended for items arising because the concern is a corporation, with funded and similar debts, regardless of the type of business it conducts. Interest on meter deposits arises because the concern is operating a utility of the type that requires meters. Therefore, customers' deposits should be shown as an operating cost, rather than a financial cost.

Advances from affiliated companies. The system of the National Association of Railway and Utilities Commissioners follows the generally accepted principle with respect to advances from affiliated companies. It provides that non-negotiable notes due affiliated companies shall not be classed as current assets while negotiable notes shall be so classed.

Intangibles. Inasmuch as the title "intangible fixed capital" is used in the system as one of the two main divisions of fixed capital, it appears that the commission does not intend that organization expense or franchise cost shall be written off regularly by a utility without specific request from the commission. Very little comment is made on the disposition of the intangible assets. In the description of the accounts themselves, no mention is made of reducing their book value. It is only from a three-line

statement under the heading of "miscellaneous amortization chargeable to income" that one learns of the possibility of writing down these assets. The lines referred to are:

> This account shall include such amounts as the accounting company may be required to charge to income in amortization of intangible book value or other items carried among its assets.

The title "good-will" is not mentioned in the classification of accounts, so far as we have observed, but there is a strong indication that the utility may set up good-will under proper conditions and report it under the general title "miscellaneous intangible capital," the description of which reads as follows:

> This account shall include the cost of patent rights, licenses, privileges, and other intangible property not elsewhere provided for; and all other fixed capital charges which are not specifically assignable to some other account in this classification.
>
> Note: When any corporation desires to reclassify, according to the uniform system of accounts, the book accounts representing its investment in plant and equipment prior to the effective date of this classification, any remainder of the original total book value over the amount determined as properly chargeable to other prescribed accounts (including profit and loss or reserve accounts in cases where it is found that part of the original total book value is properly chargeable to such accounts) may be charged to "miscellaneous intangible capital." When such a reclassification is undertaken by the accounting company (and has not been passed upon by the regulatory commission) acceptance by the commission of reports showing the revised balances shall not commit it to the approval of the amounts thus set up.

Contributions for extensions. Provision is made in the uniform system for having all fixed assets recorded at cost, regardless of the method by which they are obtained. The authors provide for this in the case of extensions of mains or lines that are paid for in whole or in part by customers, municipalities, chambers of commerce, or other organizations. Under such conditions, the full cost of construction is charged just as if the utility were paying for it in full. Then any amounts received from individuals or organizations are credited to "contributions for extensions." This account is carried indefinitely as a type of general reserve.

Appraisals of fixed property. Although appraisals are used as a basis of valuation for rate-making purposes, the uniform system does not provide for recording appraisal figures on the books of account. In the general instructions concerning fixed capital, appear the following very specific statements concerning this: "All charges to fixed capital accounts shall be at the actual cost of the property acquired, at the time of its acquisition. A *bona-fide* contract or agreement of purchase and sale between entirely separate parties shall be *prima facie* evidence of actual cost. Each item of property shall be carried in the fixed capital accounts at no more, and no less, than its actual cost unless, or until, such property is abandoned, replaced, reconstructed, or converted, when the accounting shall be as hereinafter set forth."

Residuals. Accounting for by-products may be accomplished in any of several ways. Accordingly, it is appropriate that the authors of the uniform system designated the specific method to be followed in treating by-products, or residuals, as they are called in the gas business. They prescribe the method which gives production all the benefit arising from the sale of residuals; that is, the production cost is reduced by the proceeds of sales of residuals. In order

to have each month's production credited with the approximate value of the residuals produced, whether sold in that month or not, an entry is made monthly charging "stock" account and crediting "residuals produced" with the estimated value of all residuals produced during the month. If the estimate is correct, the stock account will balance when the residuals are all sold. Any difference between the estimated value and the net amount realized from the sale of residuals is adjusted between the two accounts. This throws a slight amount (either debit or credit) into the residuals-produced account in a given month which is not applicable to that specific month. The difference, however, would usually be slight.

Any costs incurred in preparing and handling residuals for sale and making deliveries for same are charged to residuals expense account or an appropriately designated subdivision thereof. Both the residuals-produced account, with its credit balance, and the residuals expense account, with its debit balance, are "included in the financial statements under the general heading, production expenses." Thus, the net profit on residuals reduces the production cost.

Donations to charity. The authors of the uniform system apparently wanted to make it as easy as possible to adapt the system to federal income tax purposes when they provided that donations to charitable institutions and organizations for promoting social welfare should be charged direct to profit and loss account after obtaining the amount of net profit of the utility for the year.

III. Flexibility of the System

Mention has been made heretofore of the methods adopted by the authors of the uniform systems for permitting utilities to exercise options in the keeping of some accounts. In many cases the reason is obvious. In some instances, also, an option exists which is so minor in character as not to require special comment at this time. A few of the more important options allowed which make the systems more flexible from the point of view of the utilities are enumerated and discussed briefly below:

Uncollectible bills. A utility is given the privilege of charging uncollectible items to uncollectible bills account from time to time as the accounts are found to be bad, or of charging the account with only an estimated amount from month to month. Under the latter plan, a reserve is created which is charged as debts are found to be uncollectible. The treatment of collections made on accounts previously written off as uncollectible is provided for in a very satisfactory way. Such collections are credited direct to the expense account "uncollectible bills," if no reserve is used; but they are credited to the reserve account when the estimated method of handling uncollectibles is followed. The income tax regulations require a credit to bad debts recovered account under either method of accounting. In my opinion, the uniform system procedure is more reasonable when a reserve is used. The reserve is presumed to be created on a basis of experience over a period of years. This experience is the net loss from bad accounts. Therefore, if gross loss is charged to the reserve account as debts are written off, the recoveries therefrom should be credited to the reserve account in order to avoid having a debit balance in the reserve account from this cause.

Interest and dividends receivable. The utility company is given the option of settling up a current asset and income account for interest and dividends on securities held by it at the end of an accounting period or of holding such interest and dividends receivable in a suspense account until collected.

Replacement fund. Provision is made for funding the retirement reserve of a utility, as evidenced by the following sentence under the heading "replacement fund":

> If the accounting company desires, or is required, to segregate in a special fund the assets, or any part of the assets, represented by the retirement reserve, the ledger value of such assets shall be included on the balance-sheet in this account.

Property abandoned. If a utility abandons property the cost value of which is greater than the retirement reserve created therefor, the excess may be charged to profit and loss or to an account called "property abandoned." The system provides, however, that "charges to this account shall be made only with the permission of the regulatory commission, and the amount so charged shall be amortized through annual or more frequent charges over a definitely determined period to such accounts as shall be proper."

Sinking fund. Another important practice in which the utility is given an option is that of funding its sinking-fund reserves. This opinion naturally would be subject, to some extent, to provisions of trust deeds and bond indentures. Through the several accounts "sinking-fund appropriations," "income from special funds," and "sinking-fund reserves" the utility may, as it desires, or as it is required by contract to do, credit interest on sinking fund direct to the reserve or to the income account.

Self-insurance. Any utility that carries its own insurance of any kind in whole or in part may, according to the uniform classification, charge insurance account and credit casualty and insurance reserve. The method of determining the amount of such entry in any case is not described in the classification. Provision is made, also, for entries when a utility carries insurance in a mutual company.

Welfare work and pensions. The Association of Railway and Utilities Commissioners apparently observed the trend of the times in making it possible to account readily for welfare work among employees, and pensions for retired employees. Expense accounts are provided for each of these as subdivisions of general and miscellaneous expenses.

Taxes on net income. An account bearing the title "taxes on net income" is provided and it is so placed in the numbering system and in the income statement that it is the last deduction from incomes before obtaining net income or net loss for the year. This account is to be used "when such taxes are not allowed by the regulatory commission as revenue deductions in computing the 'fair' return on invested capital, but are considered to be a charge against the stockholders or other owners of the enterprise instead of an expense of the business to be transferred to the public through the prices to be charged for the service which the accounting company renders." In other words, the authors of the uniform system recognized that some state commissions might take the view of the Federal Internal Revenue Department that income taxes are a sharing of profits with the government rather than a cost of doing business. If a state commission

does consider income taxes as a legitimate element of the cost of doing business, then such taxes are chargeable to an account called "taxes assignable to gas operations," "taxes assignable to electric operations," or similar accounts for other utilities. Under the latter interpretation, income taxes would be included as an expense in calculating, from time to time, the amount which a utility must receive through rates charged to customers in order to meet all expenses of the business.

Penalty theory of discount. The following note under the general discussion of "operating-revenue accounts for gas companies" shows that a utility may use the penalty theory of cash discount and consider such discount as income in addition to net sales rather than a deduction from a previously entered gross sales figure:

Note A: If a gas corporation desires to credit its revenue accounts upon the basis of net price charged to consumers, it may be allowed to do so upon filing with the regulatory commission a notice of its intention. In such case, all discounts forfeited or penalties charged for delayed payments shall be credited to the revenue accounts involved and kept in such form as to permit their being separately reported.

Free service. From the point of view of a ready comparison of production costs, one option offered utilities is somewhat unusual. Reference here is made to the option which utilities are given of omitting entirely any charges to its several departments for service rendered by another department. For example, if a gas company uses gas in its production department, or furnishes gas free of charge to a municipality, or to employees in lieu of wages, it may refrain from making any entry for such gas disposed of. On the other hand, it may charge production, franchise requirements, or wages and credit "duplicate miscellaneous charges." The balance of this latter account is treated as one of the deductions from operating expense.

Joint costs. The question of joint costs in the case of allied utilities under one management is provided for by the following somewhat flexible provision under the heading "joint operating expenses—Cr."

When any plant or equipment is maintained or operated by the accounting company for the joint benefit of itself and others under an arrangement for apportioning the operating expenses, the portion of such expenses chargeable to others under the arrangement may be credited to this account if it is based on a percentage of the total operating expense or a percentage of the total of some group of primary operating expense accounts or determined in some similar fashion. So far as practicable, joint operating costs should be apportioned by primary accounts, and that part of such cost borne in the first instance by the accounting company, but chargeable to the other party or parties to the joint agreement, should be credited to the primary accounts involved.

Merchandise department. It is recognized in the uniform system that some utilities might carry the merchandise department merely as a means of encouraging business for the main product, while others might be so located as to make the merchandise department self-supporting. The option offered in this respect to gas companies (which is similar to those offered electric companies) is expressed in the classification under "merchandise and jobbing," as follows:

Note C: If the accounting company sells merchandise or does jobbing work at or below cost for the purpose of inducing greater use of gas, a debit balance in this account, due to such a practice, shall be charged to operating expense account number 771, "new business expenses," or the appropriate subdivision thereof.

Note D: If the accounting company is engaged in merchandise or jobbing primarily for direct profit rather than for stimulating the consumption of gas, such merchandising and jobbing may be organized and accounted for as a distinct department of the accounting company, coordinate with the gas department.

As inferred in the opening comments herein, one cannot peruse the uniform systems of accounts adopted by the National Association of Railway and Utilities Commissioners without feeling the benefits to be derived from having such systems in operation, especially for those utilities whose holdings extend into more than one state. Reports indicate that the results already obtained from the use of the new uniform systems are highly satisfactory. Good accounting principles and terminology, except in a few cases, are to be found in them, and undoubtedly they show the result of experience of accounting officers of utilities commissions in handling cases over a long period of years. These systems should play a big part in molding accounting practices and procedures in the United States.

A CHALLENGE—TO THE PUBLIC? OR TO THE REAL ESTATE BUSINESS?

By JOHN D. BLACK

AN abstraction, unless it can be reduced to a catch phrase or a slogan, is likely to have only a very gradual influence upon mankind. But a concrete manifestation will draw its followers by the thousands. One man is pinioned by a rock in a cave in Kentucky, and in a day 10,000 men have rushed to the spot! And perhaps we shall have several state legislatures passing laws prohibiting the exploration of caves except under certain conditions.

We have had abstract generalizations a-plenty of late years as to the various unsocial practices connected with the buying and selling of land. These have borne fruit in various state laws licensing real estate brokers and in the educational and ethical program of the National Association of Real Estate Boards which reaches some 20,000 brokers. But giving due credit to the efforts of the best elements in the real estate business, some sections of the land business have not been affected to the same extent by this program of raising the social and ethical level of real estate practice. Moreover, in these sections both the public and the real estate fraternity are mostly in a state of apathy on the subject—at least, in a state of too much apathy to give us hope of any considerable improvement in the immediate future.

In these circumstances, perhaps what is most needed is a series of concrete manifestations of the kind of results that present practices in backward sections are achieving. Not typical manifestations, of course, for typical manifestations seldom stir anybody to action. Hundreds of fires occur in factory buildings in which not a single life is lost and nobody is particularly excited, but with one Triangle Shirt Factory fire the whole nation is aroused.

With such an objective in view, herewith are presented descriptions of real estate results being achieved at present in two areas in the so-called cut-over region in the three Great Lakes states. The first is an area of sandy land, of which there is a plentiful supply in all three states, but especially in Michigan and Wisconsin, and the other is an area of swamp land, of which there is a plentiful supply in all three states, but especially in Minnesota. The first is taken almost verbatim from the collected field notes and subsequent summary prepared by the leader of a squad of men who made a land settlement and land utilization survey of this and 10 other areas under the joint auspices of the United States Department of Agriculture (Division of Land Economics and Land Utilization) and the University of Minnesota. The second description is summarized from similar field notes taken under similar conditions in another state.

I. The Sandy Area

The area is a single township in a county which is mostly a sandy pine

EDITORIAL NOTE: The reader will find one answer to Professor Black's "challenge" in Mr. Faast's article, "Practical Policies of Land Colonization," on page 300.

plain. On the eastern and western edges of the county are fair to good moraines of clay and sandy loam. These support four fairly prosperous farming communities now mostly in their second generation. The particular township chosen for study is mostly a dry Jack pine plain. On the north is a morainic ridge which has a slight admixture of silt with the sand. In the southeast corner is some lower land which is moist and carries a growth of cedar, white pine, balsam fir, and poplar. All the land in the township has been cut over, and all except the moist land area seriously burned over.

And yet the township has good transportation facilities. The county seat, which is at a junction of two railroads, is situated on the south line of the town.

In the spring of 1920, there were 26 families living in the township. Four of these belonged to the adjoining county seat village above mentioned and secured none of their living from the land. One family could not be located.

Self-sustaining Farms

Of the 21 interviewed, only 4 were self-sustaining on their land. Two of these live in the swampy areas in the southeastern corner. These two farms include a considerable amount of swamp pasture, which makes it possible for the owners to keep cattle. The remaining land has enough body so that with the manure from the live stock it will grow rye, oats, and clover for hay. Some posts and pulpwood are also sold. One of these farmers is a foreigner who paid cash in full at time of purchase nine years before; the other is an American who settled here over 40 years before and has accumulated 640 acres, mostly at tax sales.

Another of the four families is of foreign stock, and settled here 13 years before, on a tract close to the village. Most of the income of this family is derived from poultry, eggs, and milk. The fourth self-sustaining family is of native stock and derives most of its income from summer boarders, actually cropping in 1919 only 6 out of 400 acres. This settler has also lived in the area over 40 years. All four of these families have relied upon outside sources of income a good deal in the past, the two American families upon incomes from school teaching and county offices, and the two foreign families from road work and odd jobs. The foreigners barely escape destitution.

Status of Non Self-supporting Families

Of the remaining 17 families, 2 were not farming at all, one being a cigarmaker plying his trade in the country, and the other merely keeping his family here while working elsewhere. Of the remaining 15, all but 6 had been in the district less than a year, and were still living on the savings brought with them. None showed any promise of remaining more than a year or two. Of the remaining 6 families, 2 each had a member of the family in full-time city employment supplying the major part of the family living, and 4 were living in the swampy area in the southeastern corner and were combining outside earnings with some income from their farms.

Of the nine families who had settled in the last year, only one had begun upon land with no clearing. Two more had only several acres cleared. Some of the places had fairly substantial buildings dating back to the days when lumbering supplied the living for the region. The largest clearings in the township go back to this previous eco-

nomic period when hay, grain, and vegetables were needed in the lumber camps. One farm had 100 acres cleared in this way. Very little new clearing is being done. The new settlers mostly locate upon old farms, and seldom stay long enough to take up clearing in earnest. In the 30 years during which real estate activity has been in progress in the area, the amount of new land cleared has probably not balanced what has gone out of farming use.

Vacant Land

In addition to the 22 occupied places in the township, there were 32 vacated farmsteads with clearings ranging as high as 60 acres, and buildings in a partly dilapidated condition. From time to time, some of these 32 have been reoccupied for brief periods, and no doubt this will continue. But a good many of the 32 appear to have been finally abandoned, with oak sprouts repossessing the fields, and the houses substantially in ruins. In addition, there were identified 13 abandoned clearings of still earlier date, from which buildings and all other improvements had disappeared.

Land Transfers and Ownership

This township has never been the scene of important real estate promotion. No big selling agency has given more than incidental attention to it. And yet transfers have been numerous and continue to be so. It is doubtful if there are more than seven parcels of land in the township which have not changed hands since 1900. The majority have been sold several times since then. In 1919 alone, 36 transfers were recorded. In one section (640 acres) chosen at random, 23 transfers of title in the preceding 12 years had been recorded. This land was held in 1920 by 10 parties. This means that about one-fifth of it had been changing hands each year. The section is not touched by a road, has no clearing, and only one attempt has ever been made to farm upon it. It is all owned outside the state; one parcel in Ohio, and the rest in Illinois, mostly in Chicago. Of the 23 grantees since 1918, not one had been a local party.

Taking the township as a whole, of the 233 owners, 137 were listed as resident in Illinois, and 116 in Chicago alone; 61 as resident in the state, 40 of these in the county; and the remainder in 7 states ranging from California to Texas to New Jersey. Six parties owned a section or more each. The average size of the remainder of the holdings was 82 acres. There were many 40-acre tracts which had never been surveyed out, but had been conveyed and reconveyed.

The main factor in the frequency of sales is the apparent cheapness of the land. After the lumbering days, most of it was picked up at tax sales by tax-title purchasers who then peddled it out through newspaper advertising, largely at a few dollars per acre. Most of it probably has never been seen by the people who have owned it. It is difficult for the purchaser of such an individual tract to sell land of this sort on commission through an agent or for cash directly. The commonest form of transfer has been by trading. Houses, stores, and shops in Chicago in particular have been traded for this Jack pine sand. A not uncommon procedure has been for a tired owner of some of this land to include it as a largely fictitious partial consideration in a city real estate transaction. Wanted by neither party actually involved in the transac-

tion, the land drifts into the hands of the real estate operator who handles the deal. He then trades it for the income-producing property of some land-hungry city worker, usually in certain foreign groups. In this township the operations have been especially among Chicago west side Bohemians and Lithuanians. Other of the purchases have been in the nature of cheap speculation made by persons who never intend to occupy the land, but hope to get something for very little.

Details of Real Estate Activity

Following is a more detailed description of the real estate activity, not so much in this particular township as in the county as a whole:

1. Local Real Estate Activity. The county seat has one active real estate man. He has a connection with a Chicago firm, but apparently does not make much use of it. His business is mostly in the sale of improved farms, some in the four farm settlements mentioned, but probably mostly on the Jack pine plains. Almost all of the farms on this land are on the market, whether occupied or unoccupied. His business is not brisk. Prices are low. Farms with the usual improvements and adequate cleared land are on the market for the most part at from $10 to $20 an acre and at almost any terms. The value of the improvements, excluding cost of clearing the land, will approximate in many cases the price asked for the farm. This agent is, nominally at least, opposed to the selling of cut-over pine lands.

2. Outside Real Estate Activity.

(*a*) *Sale of tax titles.* Much land has been sold in the county for taxes, and certain buyers in particular have picked up tax titles and accumulated sizable holdings, although they rarely consolidate them. Here is the case of one such operator: He has bought much tax-title land in the western part of the state. He does not go to the trouble of perfecting title, but buys simply the taxes at the auditor general's office without going through the steps giving undisputed title. In his sales he gives merely a quit-claim deed. He is therefore able to offer lands at a low figure and still make a good profit. In 1920 he was advertising a bargain sale at prices such as $3.95 an acre. The advertisements were running in Chicago papers with the price featured and hardly any statement regarding the lands, except as to the state in which they were located.

Here is the case of another operator: This firm prepares lists showing the location of the land in several western counties in the state. If it owns the land, there is no record of it. Possibly it has optioned these tracts from several tax-title purchasers in Chicago. The records give this suggestion. The firm seems to avoid publication of any literature, but uses newspaper and magazine advertising. Last year this firm offered 10 tracts in this county lying in 6 different townships. The records disclosed that all of these tracts had been sold on tax deeds at least once and four of them twice. They had passed from the tax-title purchaser by quit-claim deed to other parties, and were therefore not quite in the nature of the offerings of the operator listed above. The actual cost to the tax purchaser was not much in excess of 50 cents an acre. They were then being offered at $11.50 and $12.50 an acre. Terms quoted were $100 down and $10 a month, on a land contract.

The history of one of these individ-

ual tracts is as follows and is rather typical: Original grant by United States to Pere Marquette Railroad, 1856; railroad to lumber company, 1888; lumber company to Chicago party, 1891 (probably cut-over). Then follow 7 warranty deeds, probably all to Chicago parties, between 1891 and 1895. The last 5 of these bear Swedish names and suggest the characteristic bartering of such land among a foreign group. In 1907 the state sold the land for delinquent taxes. The last record is a quit-claim transfer in 1911. Such quit-claim transfers not uncommonly are followed later by warranty deeds on further sales, although these deeds are no better than the grantor who issues them.

A third operator owns scattered holdings in the northern part of the county, convenient to its major operations in the adjoining county. This company is a large operator in lands of this type in this part of the state. Most of its land in this county is said to have been secured through tax-title purchases. The company gives a warranty deed, having previously perfected title. The cost of legal notices adds a dollar or two to the actual cost of the land per acre.

(*b*) *Foreign-language firms.* From time to time, real estate promotion has cropped out in some particular foreign-language group in Chicago. Little is known of these promotions until some of the purchasers arrive to make their homes in the area. The agencies apparently pick up land that is floating around in abundance in the Chicago real estate market and peddle it in small tracts. About 14 years ago, there was such an activity in the Italian settlements of Chicago, but only one of these men is left, and is now employed on the railroad. More recently, Lithuanians and Poles have been similarly canvassed by the trading method previously described. When one of these buyers has been "plucked," he is likely to return to the city and try to unload on one of his fellow countrymen.

The latest of these promotions was set forth in a Polish circular, and was under way in 1920. The supervisor of the township protested against having these people unloaded on what he called worthless land. He feared that they would become his wards. Also, this tract was so near one of the morainic farm districts of the better sort that he feared that the settlement of the Poles would ruin the free grazing which the established farmers were using to good advantage. He apparently felt that his township had reached the point of economic saturation.

(*c*) *Lot promotion.* This county affords a good illustration of a nuisance that is repeated frequently in this country—the plotting of small lots. A monotonous pine plain tract without lake, stream, or railroad passed from the Pere Marquette Railroad Company to a lumber company, then to a land speculator who grew tired of it. In 1903 it was sold for taxes. The tax purchaser sold it in 1904 to a subscription book publisher who in 1905 platted it into 400 half-acre lots. These lots were given free with a set of books. Some people bought numerous books in order to get as many lots as they wanted. Nineteen lots were recorded to California parties, 17 to Ohio, 14 to Iowa, 14 to Idaho, 11 to Colorado, and so on. Two failed to pay taxes the first year, and from that time on the tax delinquent list increased. Thirteen out of the total were still paying taxes in 1918. Twenty had dropped out the year before, and 20 a year before that. The cost of handling these lots has far exceeded their value both to state and

county. The reconsolidation of the tract is impossible as long as individuals persist in paying their taxes, and thereafter the cost of perfection of title will probably exceed the value of the property.

II. The Swampy Area

The tract of swampy land chosen for this description is wholly devoid of settlement. It could not possibly be farmed at the present time. Some of it is hardly accessible even for purposes of inspection. In its natural condition much of it is nothing more nor less than "muskeg," that is, swamp consisting of shallow water overgrown with sphagnum moss and more or less filled with somewhat decayed vegetable matter. In many places the moss and water are more than 20 feet deep. In others, the vegetable matter has mostly reached a stage of decay that entitles it to be called peat; and over broad belts around the edges of some of these swamps, the peat may not be more than a few feet deep.

Much of this land was until recently part of the swamp land domain of the Federal Government. The homestead laws require personal examination of land and residence upon it for stated periods. Residence upon most of this swamp land is out of the question. The supposition of many people has been that if it were only drained, it could be farmed. Consequently, about 1910 Congress passed the Volstead Drainage Land Homestead Act, which was intended to be a modification of the general homestead act adapting it to drainage land conditions. Thus any one with a homestead right is permitted to acquire title to 160 acres of this land without living upon it, paying the usual $1.25 per acre. Moreover, the 1910 Act permits any owners or homestead holders in any township to establish in said township a drainage district, issue drainage bonds to pay for the ditching, and levy the interest and principal payments on these bonds as annual assessments against all the land in the township, even including government-owned land. Thereafter any one purchasing a piece of this land has to pay not only the current assessments, but all delinquent assessments, with interest on the same at 12% per annum. The Federal Government, of course, becomes delinquent on all its remaining holdings in the township.

Under the terms of this act, practically all the public swamp lands in this whole region were laid out in drainage districts. The region is probably greatly overdrained, or at least prematurely drained, and the forest-fire hazard has been greatly increased in consequence. Promoters made a business of creating drainage districts and selling the bonds. Many of them were sold considerably under par. No doubt the drainage contractors also profited greatly from this activity.

Real Estate Activity

Lastly, the present policy has furnished a splendid opportunity for that species of real estate practitioner who calls himself a "locater." The following excerpt from the advertising literature of one of the "locaters" illustrates the methods and tactics employed by some of them:

> We positively guarantee that these complete reports and plats now shown at our office contain all the information required to enable us, who are thoroughly familiar with them, together with the applicant after he comes to our office, to select the best and most valuable tract of government land obtainable on the day the applicant or his application arrives at our office. It has taken many years of expert professional work, in-

volving a great expenditure of money, to obtain all the absolutely accurate information contained in these reports and plats, but when all this vast information is acquired and these plats are complete, same enables us then to absolutely guarantee to each and every prospective purchaser that we, in 10 minutes, can and will make, all things considered, a better selection at our office for our customers than can possibly be made by a hurried trip to the land by the average landseeker or any one else not having the knowledge we have of the government lands, and thus every common-sense landseeker can, and will, buy this land from the government through our office with utmost confidence and with absolute assurance of getting the best land there is to be had without going to see the land for himself.[1]

The fact is that the only service rendered is to select on a map a piece of muskeg or peat land which contains no timber of importance. "For this service, and for inducing the victim to assume the burden of taxes and special assessments, amounting to from $25 to $40 a quarter section, the charge is from $560 to $680 a quarter section in the case of a typical concern of this kind. These prices include the back taxes paid by the company,"[2] and the $1.25 per acre paid to the government.

Present Real Estate Situation

To complete the picture, it only needs to be stated that practically all of the federal swamp lands in this whole region have been sold at least once on this basis, and some pieces have already been sold two or three times. At present writing, almost a third of the tax descriptions in one whole county in this region are reported as delinquent. This means that the buyers of it have discovered the nature of their investment, or have grown tired of paying the heavy drainage assessments, and are letting their land go upon the delinquent-tax market, to be purchased again by the "locaters." The "locaters" seem to be doing as thriving a business buying up "relinquishments" or tax-sale lands and reselling them as they did selling the land the first time. It looks as if the process could continue for a long time to come unless checked in some way. For who is ready to say when this land will pass out of the sub-marginal class?

Who have bought these lands? Many have been actual prospective settlers—not prospective in the near future, of course, but in the next 10 or 20 years. A surprising number of them are farmers in the Corn Belt who are buying these lands expecting them presently to become rich farming lands as have some swamp lands in their neighborhoods. Some of these are thinking particularly of providing land for their oncoming sons. Other buyers are city-workers with a back-to-the-land notion lodged somewhere in their heads. They are thinking that they will at least have this to turn to in their old age. Many other buyers, however, are more nearly speculators than these classes that I have mentioned.

Some of the real estate men who deal in lands of this type justify their business on the ground that they are not selling it to actual settlers, but instead to persons who expect to get something for nothing, and they consider such persons fair game. This, it will be apparent, is only a partial truth. Many, indeed, of the buyers are potential settlers.

III. Remedies

It is not the purpose of this article to suggest remedies for the conditions that

[1] *Settlement and Colonization in the Great Lakes States,* United States Department of Agriculture, Bulletin No. 1295, pp. 81-82.

[2] *Ibid,* p. 82.

have been described. The writer wishes, however, to make a few observations on this point. The first of these is that there is not much that is now being done by the real estate fraternity in these sections, by the Federal Government, or by any of the states, that is making any particular impression upon conditions such as have been described. Except in a comparatively few places, the objectionable practices are going on unabated. There is a tremendous amount of land in the United States that lends itself to such practices; and there is a tremendous number of persons who are potential subjects for such victimizing; and there seems to be no decline in the number who are willing to be the middlemen and bring the two together. Real estate licensing procedure will have to be more rigorous than it is now before it will remedy the situation. Likewise state commissioners of immigration will have to conceive their tasks upon broader lines than most of them do. And real estate bodies will have to bring into these backward sections their higher standards of business and social ethics. And perhaps all these will not be enough.

PRACTICAL POLICIES OF LAND COLONIZATION

By B. F. FAAST

AMERICA'S history is filled with the thrills of frontier life. It is a history of exploration and pioneering. For three centuries American people have been pushing westward, engaged in a struggle to conquer the wilderness. The prairie-schooners, caravans, Indians, and all the colorful but strenuous life that went with them, are now things of the past. The old frontier has been pushed westward and northward until it has almost disappeared into the Pacific Ocean and behind the Arctic Circle.

A new frontier still remains, however, in the arid lands in the West, swamps in the South, and forest lands in the North, South, and West, which home seekers and "empire builders" passed by in their forward march to conquer the prairies. In these sections today we have the nearest approach to the frontier of yesterday. Here the modern pioneers are building their new farms and towns, and establishing business and industry. Constructive land settlement does not mean merely opening new farms, as is so often thought. Industry and business must develop jointly with the new farms. Town and country are dependent, one on the other, and in planned communities the pioneer merchants, manufacturers, and farmers work together in the common cause of community building.

The Old Pioneer Spirit Still Lives

The question is often heard, "Why settle new lands as long as there are deserted farms in the old, settled regions?" "Why not reoccupy the abandoned farm homes and inject young blood in these non-progressive districts?" This policy has been tried time and time again. History has given the answer. These farms were abandoned partly because they became unprofitable in competition with newer and more fertile lands and partly because of the desire to have a share in the building of a new country.

Yet the pioneer spirit which prompted the opening up of new lands and the abandonment of farms in other regions still exists. America is filled with optimistic young men and women who long to start life in a new country where they can play a larger part in the doings of things, where their neighbors have the same ideals and ambitions, where all start on an equal basis, and where creating, planning, and hard work earn a rich reward. The pioneer plays an active part in community building. The schools, the town government, the roads, the cooperative enterprises, the banks, the local industries, all are the result of the thought and labor of some group of pioneers.

In the older communities business institutions are established, the "old-timers" are in control of school and town affairs, traditions, and customs; and the well-known, self-satisfied atmosphere stifles the ambitions of the younger men and women who want to do things a little differently and a little better. Is this not one of the answers as to why the future farmer, like the

business and industrial leader, is ever seeking new lands? Is this not one of the reasons for the remarkable progress of America? Until the old farming districts catch the spirit of young America and are willing to rebuild town and country, the best of America's youth are going to search for and demand pioneer land-settlement projects, where town and country are in the making, and where a new agriculture and new industry are being created.

The opportunity for home ownership is greater in the new countries and new regions, for there owned homes can be secured with but little cash and on favorable terms. Labor and creative leadership is the price of home ownership, and most young men and women are willing to labor and plan in order to secure a home in a country which they have helped to build. This continuing pioneer spirit explains much of America's rapid development in the past; it explains, in large measure, the present-day eagerness to settle the modern frontier.

To meet this demand for new farms on the frontier, various policies, some good, some bad, have been practiced. The modern colonization company is as different from the old land selling agencies as the modern frontier is different from the frontier of yesterday. Experience has taught that it pays, in the long run, to use methods which two generations ago might have been derisively called "social uplift." The modern colonization company pays more attention to scientific methods than to rule-of-thumb practices. This is merely one difference among many. It is impossible, in the short space of an article, to describe all the current practices and why they were adopted; it must suffice to point out a few outstanding, practical policies of modern colonization.

Economic and Soil Surveys

Before any large tract of land is blocked into farm units and sold to home makers, a detailed soil and economic survey should be made to determine for what the land is best adapted.

While the productive power of the soil is one of the first essentials for successful farming, it is of equal importance to determine what crops can be marketed at a profit. Certain soils may produce big yields; but there may be no market for the crop, or the freight-rates may be prohibitive. It is therefore essential that in addition to the analysis of the soil an economic survey be made, so that the farmers will know what kind of farm produce the market will absorb at a fair profit. New markets and new crops should be studied. Instead of producing only foodstuffs, our farms should grow more raw materials for our manufacturing plants. Here is a field that has hardly been touched by the farm economists.

Lands not suitable for land settlement, such as submarginal, non-available, or surplus good lands, should be utilized for reforestation, grazing, or recreational purposes. These lands will then be conserved as potential homes for succeeding generations of home seekers. If only the good available farm land were opened for planned land settlement, there would be no surplus farm land and no cause for the cry of "overproduction."

The Department of Commerce advises manufacturers and jobbers as to the demand and supply for the products of the industry. Many trade and commercial organizations furnish this kind of information to their members. Business statisticians and analysts, such as Babson and Moody, issue weekly service letters to their subscribers. Farm or-

ganizations must also make economic surveys and keep their members advised as to the market conditions. It may be desirable to have federal and state agencies work in cooperation with such groups as the American Farm Bureau, the National Council of Farmers' Co-operative Marketing Associations, and the other farmers' organizations.

From whatever reliable source such information comes, it is important to have these data, in order to make a wise selection of the land and a division of the tract into proper-sized farms. All this information bears upon the earning capacity of the land, upon which so much of the success of the settlement depends.

Colonization Is Replacing "Just Selling" Methods

The demands of the farm seekers of today are slowly but surely forcing a change in the method of land selling. In place of the old-fashioned land office with nothing to sell but a title to a piece of land, there has come the modern land-settlement company, with well-planned communities, good roads, attractive farm buildings, good market centers, farmers' cooperative associations, and service to the farm buyer as one of the outstanding features of the sales plan. Land settlement should mean more than mere selling of a piece of land.

The Example of City Planning

Not so many years ago, the city real estate men learned that in order to attract families to the industrial centers, it was necessary to do more than just sell a lot. Subdivisions were carefully platted, parks and playgrounds provided, utilities installed, and modern homes erected. Finance corporations were organized to sell these homes on the long-time payment plan. State legislation and municipal ordinances gave aid and encouragement to the home-owning movement. Nearby factories furnished a market for labor. The success of these modern subdivision projects has proved the soundness of this method of constructive development and liberal sales policy.

This same planning, building, rendering of service, and long-time credit must be a part of every successful land-development project of the future. The men and women of today will never go back to the old pioneer conditions of 50 years ago. Modern methods must be applied to farm and community building, just as they are now being applied to the rebuilding of our cities.

Rural Planning

The soil and economic survey will determine the size of the farm units to be sold, the location of the highways, schools, social centers, rural parks, towns, and the kind of farming to be followed. After the roads are built, schools and community centers constructed, towns laid out and started, then comes the work of bringing in new families and locating them on their new farm and town homes.

Under the colonization plan of settlement, an attractive, yet inexpensive, house and a barn are usually built on each farm unit. The general appearance of a new country where the small farm cottages have architectural character and are attractively painted, and where a few trees, shrubs, and flowers frame the homestead, is in striking contrast to the average tar-paper shack and log cabin of the beginner in unorganized and isolated settlements.

The Importance of Credits and Their Amortization

The majority of land-settlement organizations provide for the credit needs of their new farmers. It requires capital to reclaim, develop, and equip a farm home out of raw land. The developing organization provides the credit necessary for reasonable development of farms to the point of profitable export to market. The credit terms are as important as the amount of credit.

Any successful system of farm credits must grant loans for such a length of time as will allow repayments from the earnings of the farm. If 30 to 35 years is deemed the proper length of time for a federal farm loan on the amortization principle, it is all the more necessary that an equal or longer term credit be granted to the new farmer, who must reclaim, improve, and equip his farm before he reaches the stage of export production. All capital loans advanced for improvement purposes should be made on the amortization plan for a period of 30 to 40 years, with no payments for the first 3 to 5 years. This credit, so important to the success of the beginner, is usually provided only by organized development and selling agencies. The new farmer who buys land from some individual is too often deprived of the advantages of the kind of credit he most needs.

Land Plus Service

Everywhere in business the word "service" stands out as a measure of value. Service in country building means careful community planning, and division of the land into the most economical farm units. Service also means that the seller helps the new home owner in the development of his farm. But what of the family that buys land in some distant, unorganized frontier? The contrast is marked—no nearby school, few neighbors, no leadership, a log house that takes all summer to build, no advice on pioneer problems, and no credit advanced at a time when a few dollars mean the difference between success and failure. A countryside not planned must some day pay the cost of rebuilding.

The new colonization plan gives assistance to the beginner when help is most needed. The colonization truck or team meets the family at the station, drives them to their comfortable new cottage, all ready to occupy. They have neighbors, schools, and a church. The Community Club visiting committee calls on the newcomers and helps them get acquainted with the neighbors, and they are invited to attend the social gatherings at the community center. Yes; service is worth while, and the modern pioneer is willing to pay for it.

Planned Towns Are Important

The average small country town is a sad example of lack of planning—narrow streets, few, if any, parks, poor architecture, and inefficient merchandising. Our rural towns are the business and social centers of the surrounding community, and should be made just as attractive as are the new subdivisions of our growing cities. The American small town should serve as the front yard or gateway to the country.

Many of our old American cities are being rebuilt; miles of streets are being widened; whole blocks are wrecked to provide for new buildings, parks, and playgrounds. Such is the spirit of industrial America. Our small towns and country districts must follow suit.

"Main Street" must go. New, carefully planned towns on the frontier will gradually force old-fashioned villages to rebuild and modernize. The automobile, radio, and flying machine are tending to unite farm and city, and no land-settlement project can be successful without town and country being planned and developed jointly.

Upon the careful selection of new farmers who have the ability to "make good" depends the success of any colonization project. After all, the personality of the pioneer men and women is as important as the plan of settlement. One advantage of the carefully planned community with the service features emphasized is that it will generally attract the most desirable families. Ambitious men and women with high ideals want attractive homesteads in a progressive neighborhood, and prefer not to move into the "backwoods" or into the abandoned farm districts, if they can find a planned community that is rapidly developing and has the social advantages which modern farmers feel that they deserve.

Land Settlement Creates New Market

The settlement of new lands not only provides desirable homes for the homeless, but also creates a market for the products of our industry and the surplus of our farms. Instead of increasing agricultural production undesirably, the settlement of cut-over timberlands furnishes a new consuming market. Every pioneer region, during the early period of development, is an importing rather than an exporting country. During the first 10 to 25 years these new frontier districts furnish a market for building materials, farm tools, machinery, food, clothing, live stock, and feeds. Systematic land settlement is a real asset to any state, and should be encouraged.

Taxation of Vacant Lands

In some quarters objections are raised to the private holding of unused lands, disregarding the economic necessity of this policy under some circumstances. Instead of increasing taxes on vacant land so as to force sales, a plan of taxation should be adopted which would tend to conserve these lands for use as the need for new farm homes calls them onto the market. In the meantime, they should be taxed on a valuation based upon their present highest potential use. Much of the so-called unearned increment on vacant lands is more of a theory than a fact. Excessive taxation of timber lands is largely responsible for the slashing of our forests, which has resulted in the present shortage of timber. Do we want to repeat this mistake and likewise waste our agricultural frontier?

Forcing land onto the market by confiscatory taxation will not solve the land problem, nor will it aid the pioneer farmer. "Just selling" has been the mistake of the past. We need soil and economic surveys, rural planning, the community type of land settlement, and a fair method of taxation.

The Frontier a National Asset

From the humble homes of the pioneers of today and of tomorrow will come the future leaders in agriculture, business, and industry. Let us then conserve and protect one of our greatest remaining assets—the American frontier—and adopt a policy of constructive cooperation between the government and the private organizations so that our vacant lands will be developed at the time and in the manner that will best serve the interest of the nation.

PUBLIC UTILITY FINANCING, 1919–1925

By HERBERT B. DORAU

MANY facts bear evidence to the growing importance of the public utility industries. The every-day dependence of all upon one or more of these enterprises is accepted and no longer impressive. Only when more detailed attention is given to the tremendous growth of these new industries, does one appreciate the important place that the public utility fills in our industrial system.

The growth of public service industry can be illustrated in a great many ways. Whether one examines growth of capitalization, number of employees, gross revenues or expenditures, the remarkably rapid growth of these industries during the twentieth century can be seen. As might well be expected, public service companies have grown more rapidly than any other important industries. Railroad and industrial investments have successively held a dominant market position. However, the accumulating evidence of the last few years seems to point to an era in which investments in public service industries will be in the front rank of popularity and importance.

The Increased Volume of Public Utility Financing, 1919-1925

The period 1919-1925 is a span of six years during which the growth of public service industries has been particularly rapid. During 1924 the new security issues of public utility corporations in this country reached the impressive total of one and a half billion dollars, a sum just less than 40% of all corporate security issues of record.

During the years 1919, 1920, and 1921 the volume of new public utility security issues averaged about a half-billion dollars par value annually (Table I). The year 1919 was one of uncertainties, while the high interest rates prevailing during 1920 and 1921 precluded any great expansion. The rise in the price of utility security issues during and after 1921 (Chart VII), due to falling interest rates and rapidly reviving confidence in the stability of the utility industries, encouraged the issuance of a greatly increased annual volume of securities during the years 1922, 1923, and 1924. Total issues during the last three years represented more than twice the volume of the years 1919-1921 and represented 69% of the grand total of public utility security issues of record during the six-year period. During 1924 the total par value of new public utility security issues of record reached $1,529,639,827. If the volume of new issues during the first quarter of 1925 may be accepted as evidence, the peak of utility financing has not yet been reached. The volume of new public utility securities issued during the first quarter of 1925 was, according to the records of the *Commercial and Financial Chronicle*, $614,605,725, a volume larger than for any quarter during the entire six-year period under survey, and comparable to the yearly totals of 1919, 1920, and 1921.[1]

[1] The source of the basic statistics for this analysis is uniformly the monthly record of new capital flotations of the *Commercial and Financial Chronicle*. The source is generally accepted as depend-

TABLE I. VOLUME OF NEW PUBLIC UTILITY SECURITY ISSUES BY MONTHS, QUARTERS, AND YEARS, 1919-1924*

	1919	1920	1921	1922	1923	1924
January	$119,368,600	$ 80,431,000	$ 65,760,400	$ 55,449,650	$ 145,879,286	$ 133,532,000
February	56,943,000	32,875,940	29,563,000	56,603,525	78,706,600	105,997,700
March	29,495,600	32,625,500	30,307,090	51,747,000	112,398,800	93,510,250
First Quarter	205,807,200	145,932,440	125,630,490	63,860,175	336,984,686	333,039,950
April	6,049,000	45,508,000	30,424,000	59,979,000	76,135,000	134,284,000
May	18,079,000	45,597,900	42,300,000	179,633,800	78,384,950	278,639,000
June	31,344,000	23,944,400	11,250,000	115,131,500	110,406,300	145,507,250
Second Quarter	55,472,000	115,050,300	83,974,000	354,744,300	264,926,250	558,430,250
July	49,251,200	30,085,000	136,900,500	51,949,300	25,080,000	124,364,512
August	24,081,500	13,708,800	38,911,000	25,693,220	47,457,050	74,131,400
September	64,835,000	52,647,000	40,266,000	175,809,500	40,715,120	91,468,000
Third Quarter	138,167,700	96,440,800	216,077,500	253,452,120	113,252,170	289,963,912
October	29,120,000	39,095,300	39,533,000	92,016,750	70,634,500	133,280,480
November	9,979,750	24,770,650	142,266,880	51,700,800	418,447,480	82,017,835
December	23,725,000	75,533,060	63,603,350	64,659,750	243,367,569	132,907,400
Fourth Quarter	62,824,750	139,399,010	245,403,230	208,377,300	423,233,052	348,205,715
The Year	462,271,650	496,822,550	671,085,220	980,433,795	1,138,396,158	1,529,639,827

*Including all classes of interest-bearing securities and all classes of stock. Security issues of steam railways are not included. Compiled from the monthly record of new capital flotations of the *Commercial and Financial Chronicle*.

Examination of the monthly volume of financing during the last six years displays no regularly repeated variations (Table I). December and January are most consistently the high months of the year, while August is on the average the lowest month. By scoring each month 1, 2, 3 as it was the largest, second largest, and so forth, and adding the scores, the following average trend over the six-year period is observed:

January	18	July	43
February	42	August	63
March	47	September	35
April	41	October	38
May	29	November	45
June	37	December	28

During this period of six years and particularly between 1921 and 1924 the changes in the total financing were so great that any normal seasonal change was submerged by the sudden changes in total volume.

(Footnote 1 continued from page 305)

able. With respect to the limitations of the records the compilers explain as follows:

"Our purpose in these tabulations is to cover the new stock and bond issues of the entire country. While we aim to make our statements very comprehensive, we strive nevertheless to guard against swelling the totals beyond their true magnitude. Size is not our aim and large totals in themselves furnish no criterion of either accuracy or completeness. Unless care is exercised to exclude all issues except such as actually find a market, the totals are likely to run too large rather than too small —that is, to exaggerate the new capital demands instead of reporting them inadequately. It is proper to mention that though our purpose is to cover the entire country, it is obviously out of the question to include every stock or bond that may be put out. Minor issues, of course, have to be ignored, since otherwise the task would be altogether too stupendous, and furthermore the sources of information for the purpose are lacking. If, for instance, a small private corporation puts out a $25,000 or a $50,000 bond issue, and the new obligations are taken entirely by insiders, knowledge regarding the matter in the great majority of cases is not likely ever to come to public notice. However, the omission of insignificant issues of this kind is of little or no consequence, since the sum total of them all will never reach any great aggregate.

"A more important matter in our estimation is to eliminate the issues that are never carried to success. At times offerings are only tentative and when they do not meet with success they are withdrawn and some other means employed of obtaining the money desired. In order to indicate in a general way the plan we are pursuing in our compilations, we should say that we make every effort to limit our statements to such securities

TABLE II. SUMMARY OF GOVERNMENT AND CORPORATE FINANCING, 1919-1924*

	1919	1920	1921	1922	1923	1924
Grand Total.....	$4,286,188,860	$4,010,048,184	$4,203,793,085	$5,244,862,294	$4,989,745,599	$6,327,085,941
Government—Total†...	1,546,535,214	1,043,743,487‖	1,812,885,274	2,171,579,847	1,756,905,502	2,488,514,877
Corporate—Total	2,739,653,646	2,966,304,697	2,390,907,811	3,073,282,447	3,232,840,097	3,838,571,064
Public Utilities.....	462,271,650	496,822,550	671,085,220	980,433,795	1,138,396,158	1,529,639,827
Railways (Steam)....	208,117,000	377,879,500	655,288,500	651,531,350	518,249,450	940,296,969
Industrials‡.....	881,341,460	1,063,139,273	440,075,925	567,503,552	820,821,529	507,818,272
Other Corporate§.....	1,187,923,536	1,028,463,374	624,458,166	873,813,750	783,672,951	709,259,596

*Compiled from the records of the *Commercial and Financial Chronicle*.
†Includes Farm Loan and War Finance Corporation issues.
‡Iron, steel, coal, copper equipment, motors, accessories, and other industrial and manufacturing.
§Oil, real estate, rubber, shipping, and miscellaneous.

The Volume of Public Utility Financing Compared with the Volume of Other Financing

Only when compared with the total financing and particularly with all corporate financing during the years 1919-1925, does the relative importance of the demand for capital by public service industries become apparent. During the six years under survey the grand total of public and private financing of record increased. Government borrowing varied comparatively little, as shown in Table II, while financing by industrial corporations generally declined in volume after 1920. The large amount of real estate financing during recent years was the important factor in maintaining the volume of "other corporate" financing.

In 1919, public utility financing represented 10.8% of all government and corporate financing; in 1920, 12.4%; in 1921, 16.0%; 1922, 18.7%; 1923, 22.8%, and in 1924, 24.2%. When the volume of new public utility security issues is compared with the volume of all corporate financing, both the increase in volume and relative importance are more striking (Chart II). In 1919, public utility issues represented 16.9% of all corporate issues of record; in 1920, 16.7%; 1921, 28.1%; 1922, 31.9%; 1923, 34.9% and in 1924, 39.8%. During the first quarter of 1925, new issues of public utility securities represented in par value 45% of all corporate issues of record. Since 1921 the financing of steam railways and other public utilities in each year constituted over half of the par value of all corporate issues. In 1924, for instance, 65% of new corporate security issues were by railway and public utility corporations.

(Footnote 1 continued from page 306)

offered in the United States as actually pass beyond the issuing corporation's control for a monetary consideration. In pursuance of this practice our statements are rigidly restricted to the following:

"1. Issues which the offering bankers stated they had purchased or underwritten;

"2. Issues which, while it was not directly claimed were purchased or underwritten, were offered by such banking houses as to give practical assurance of a definite commitment on their part;

"3. Subscription privileges extended to shareholders where the right to subscribe to additional stock was of such value as to make the taking of the additional stock a practical certainty;

"4. Offerings by a corporation of its own securities direct where assurance was to be had that the securities had been sold.

"On the other hand, offerings of the following nature have been excluded:

"1. Offerings by brokers where it was uncertain if issues were underwritten or only being sold on a commission basis and amounts disposed of were not known;

"2. Offerings by corporations of their own securities, direct, where it could not be ascertained whether or not the same had been sold.

"Stated in brief, our totals embrace merely definite and tangible flotations—those that actually found a market and passed into the hands of investors and bankers, or were taken by the owners of the enterprise." (*The Financial Review* (1921) pp. 83-84).

TABLE III. GROUPING OF NEW PUBLIC UTILITY SECURITY ISSUES BY CLASSES OF SECURITIES AND PURPOSE OF ISSUE, BY YEARS, 1919-1924*

	1919	1920	1921	1922	1923	1924
Total—All Classes	$462,271,650	$496,822,550	$671,085,220	$980,433,795	$1,138,396,158	$1,529,639,827
New Capital	278,837,750	382,339,052	491,934,940	726,241,509	887,990,729	1,325,600,827
Refunding	183,433,900	114,483,498	179,150,280	254,192,286	250,405,429	204,039,000
Long-Term Bonds, Notes, etc.	173,792,000	218,048,100	473,205,000	632,406,000	812,188,100	880,110,900
New Capital	117,046,000	199,998,100	349,975,000	431,081,339	588,821,471	722,018,123
Refunding	56,746,000	18,050,000	123,230,000	201,324,661	223,366,629	158,092,777
Short-Term Bonds, Notes, etc.	252,424,700	218,065,500	72,235,000	45,756,000	64,675,000	128,073,000
New Capital	126,480,800	127,026,252	24,872,000	19,445,000	48,712,200	107,032,000
Refunding	125,937,900	91,039,248	47,363,000	26,311,000	15,962,800	21,041,000
Stock	36,054,950	60,708,950	125,645,220	302,271,795	261,533,058	521,455,927
New Capital	35,304,950	55,314,700	117,087,940	275,715,170	250,457,058	496,550,704
Refunding	750,000	5,394,250	8,557,280	26,556,625	11,076,000	24,905,223

*Compiled from the monthly record of new capital flotations of the *Commercial and Financial Chronicle*. Steam railways are not here included in "public utility."

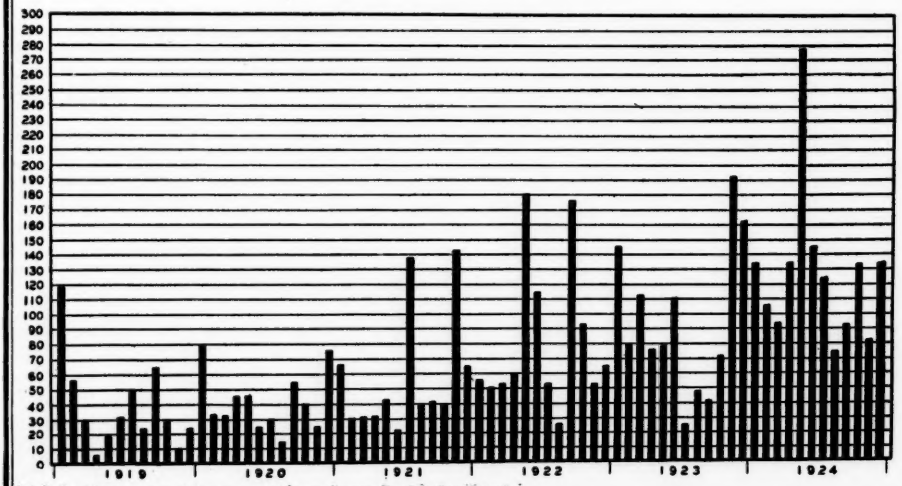
New Capital or Refunding Issues

It is of some importance to determine whether the generally increased volume of public utility security issues represents merely concerted refunding of short-time securities, issued during high interest rates, or whether the new issues are primarily for raising new capital for the expansion of the industry. Examination of the reported purposes of new public utility security issues makes possible an estimate of the amount of financing for refunding and of the volume of new securities that represent an increased investment in the industry.[2] No overwhelming proportion of the new capital flotations was

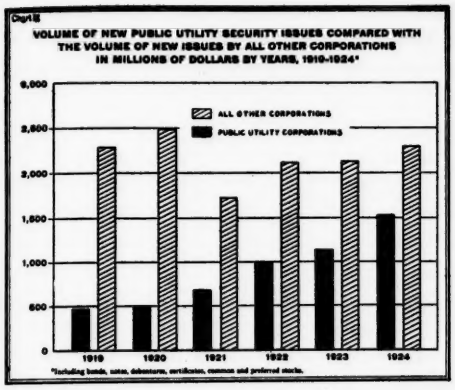
[2] The division of security issues into the two classes "new" and "refunding," as made in the compilations of the *Commercial and Financial Chronicle*, is adopted for this purpose.

Chart 1

VOLUME OF NEW PUBLIC UTILITY SECURITY ISSUES IN MILLIONS OF DOLLARS BY MONTHS, 1919-1924*



*Including bonds, notes, debentures, certificates, common and preferred stocks.



for refunding purposes (Table III) even during the years 1919 and 1920 when the volume of new public utility security issues was comparatively small and the cost of money high and when only refunding or most pressing needs might be expected to be cared for. In 1919, 39.7% is estimated to have been for refunding. In no subsequent year did the proportion for refunding rise to as high a figure; 23% in 1920, 26.7% in 1921, 25.9% in 1922, and 22.0% in 1923 represent comparatively constant proportions. In 1924, however, when the total volume reached a billion and a half, only 13.3% was for refunding purposes (Table IV). Large refunding operations might well be expected, however, during the first quarter of 1925, yet of a total par value of $614,605,725 only 12.9% was reported to be for refunding purposes. In anticipation of a lower cost of money, most of the refunding issues during 1919 and 1920 were for short terms; in 1921 and thereafter refunding issues were mostly for a longer term of years.

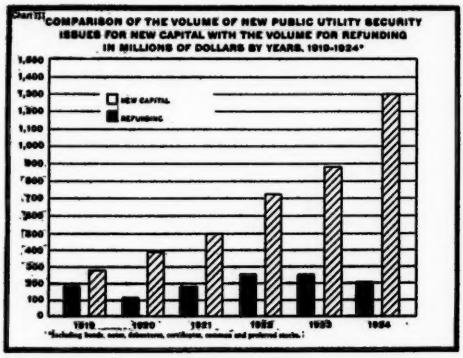
Long- and Short-Term Financing

The changing proportions of long- and short-term financing are set forth in Chart IV and Tables III and IV. After 1920, with rapidly falling interest rates, the chief motive for short-term financing was no longer controlling. During 1924 only 8.4% of the total par value of securities issued was for a term of five years or less. In the first quarter of 1925 almost the same percentage of the total par value of all types of securities (8.2%) was for periods of 5 years or less. In Table IV the proportion of short- and long-term financing

TABLE IV. PERCENTAGE DISTRIBUTION OF NEW PUBLIC UTILITY SECURITY ISSUES, BY CLASSES, 1919-1924*

	1919	1920	1921	1922	1923	1924
Total—All Classes	100.0	100.0	100.0	100.0	100.0	100.0
New Capital	60.3	77.0	73.3	74.1	78.0	86.7
Refunding	39.7	23.0	26.7	25.9	22.0	13.3
Long-Term Bonds, Notes, etc.	37.6	43.9	70.5	64.5	71.3	57.5
New Capital	25.3	40.3	52.2	44.0	51.7	47.2
Refunding	12.3	3.6	18.3	20.5	19.6	10.3
Short-Term Bonds, Notes, etc.	54.6	44.0	10.8	4.7	5.7	8.4
New Capital	27.4	25.6	3.7	2.0	4.3	7.0
Refunding	27.2	18.4	7.1	2.7	1.4	1.4
Stock	7.8	12.1	18.7	30.8	23.0	34.1
New Capital	7.6	11.1	17.4	28.1	22.0	32.5
Refunding	.2	1.0	1.3	2.7	1.0	1.6

*Compiled from the records of the *Commercial and Financial Chronicle*.



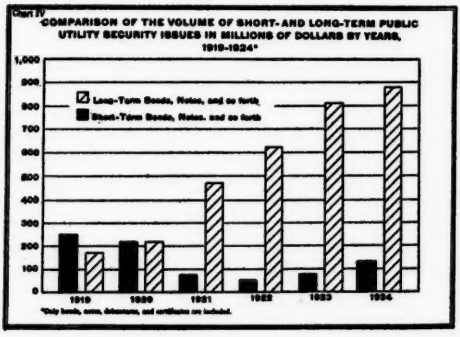
is expressed as a percentage of the par value of all types of securities, that is, bonds, notes, debenture certificates, common and preferred stock. When stock issues are excluded from the base of calculation the following somewhat different relations obtain: Long-term bonds, notes, debentures, and certificates were 40.8% of the total of all interest-bearing obligations, in 1919; 49.9% in 1920; 86.7% in 1921; 93.2% in 1922; 92.6% in 1923; and 87.3% in 1924. During the first quarter of 1925, 89.4% of the par value of all interest-bearing obligations was for periods longer than five years.

Proportion of Stocks to Bonds

During the years 1919-1921 only a few public utility companies found it desirable or possible to raise new capital by the issue of stock. With interest yields on bonds at extraordinary levels, the cost of capital through stock issues was generally prohibitive. During 1919, 1920, and 1921 the par value [3] of stock issues of record represented only 7.8%, 12.1%, and 18.7% of the total volume of financing. With the reestablishment of lower interest levels in 1922, 1923, and 1924, the proportion of the value of stock issues to total volume rose markedly, representing, in 1922, 30.8% of the volume of all financing, in 1923, 23.0%, and in 1924, 34.1%. Over the six-year period 25% of the total volume issued was stock.

The small proportion of the financing which could be in the form of stock issues during the first years of this period accounts partly for such a low proportion. It should also be noted that stock issues are very largely for new capital, while no inconsiderable part of the issues of interest-bearing obligations was for refunding purposes. When the comparison is between stock for new capital and all issues for new capital, the percentage of value of stock issues to the total for the six years is 30%.

The impression prevails that most of the stock issued was preferred rather than common. But, while there has been a great increase in the volume and popularity of the public utility preferred stock, further analysis shows that over this six-year period 46% of the value of stock issued was preferred and 54% common. If telephone and telegraph company issues are excluded, the proportion of preferred stock to all stock issued during 1919-1925 was 63% instead of 46%. This difference is due to the fact that telephone and telegraph company stock issues were 79% common and 21% preferred.

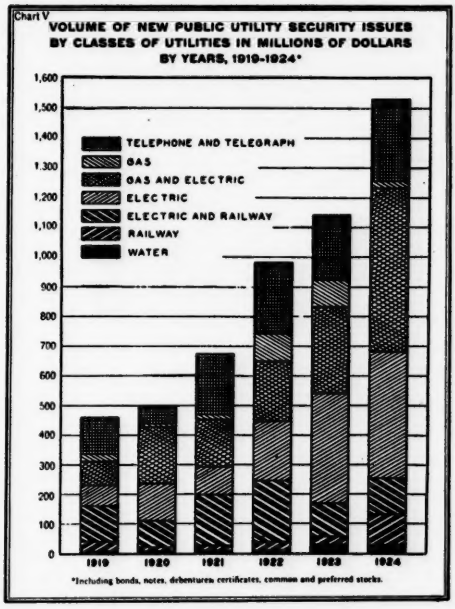


[3] Par value or amount involved in case of no-par-value stock.

Volume of Financing by Classes of Utilities

A classification of public service corporations is difficult to make. Almost every conceivable combination of services can be found rendered by one corporation. Such a classification will tend either to be arbitrary and not entirely consistent, or else to have so many classes as to be useless.

For purposes of further analysis of the financing of public utilities in the United States during the period 1919-1925, the following classification of public service corporations has been made. Being limited in number for practical reasons, this classification must at some points leave much to be desired, but it probably is satisfactory for the purposes in mind. In Class 1 are included all telephone and telegraph companies. This utility is rarely combined with others and so presents no particular problem. When, for instance, a power company operates a telephone line as a plant facility and also for public service, such an exceptional combination is treated as electric and the telephone utility disregarded. In Class 2 are included all corporations supplying gas service exclusively; in Class 3, corporations supplying gas and electric service; in Class 4, corporations supplying only electric service; in Class 5, those providing electric railway service and electric service. In Class 5, however, are also included corporations which render some other service besides railway and electric. This is exceptional, but occasionally gas service, water supply, or heating service are also provided by these companies. In Class 6 are placed those corporations rendering electric railway service exclusively, and in Class 7 those corporations exclusively furnishing a water supply. Not infrequently electric power companies also supply water, but generally this is a very minor aspect of the business, and the corporation is classed as "electric."



In order to arrive at an estimate of the proportion of the volume of new public utility issues assignable to each class of utility, every security issue of record was related to the issuing corporation and the character or combination of services rendered determined by consulting Moody's *Public Utility Investments*. This involved an analysis of the character of the corporations selling 1,244 different security issues. On the basis of this classification there is presented in Table V a distribution of the new security issues for each year, 1919-1925, by classes of utilities. The percentage distribution in Table VI and the distribution by volume in Chart V indicate the relative importance of these various classes.

The telephone and telegraph utilities accounted for a considerable portion of

TABLE V. DISTRIBUTION OF NEW PUBLIC UTILITY SECURITY ISSUES ACCORDING TO UTILITY CLASS OF ISSUING CORPORATION, 1919-1924*

Utility Class	1919 Par Value†	1920 Par Value	1921 Par Value	1922‡ Par Value	1923 Par Value	1924 Par Value
Telephone and Telegraph	$123,915,000	$ 60,426,150	$198,991,610	$242,389,900	$ 213,025,000	$ 273,546,600
Gas	22,810,000	10,977,450	14,962,000	82,880,425	91,399,787	25,305,000
Gas and Electric	80,428,550	191,677,350	162,352,403	201,630,920	291,379,306	549,453,615
Electric	72,674,000	126,388,100	94,493,207	200,589,400	373,927,265	422,042,850
Railway and Electric	122,734,100	87,990,000	174,077,000	205,700,600	110,049,800	123,402,750
Railway	35,500,000	13,538,000	18,160,000	27,744,000	26,885,000	103,268,000
Water	4,210,000	5,825,500	8,049,000	8,201,500	31,430,000	30,307,012
All Utilities	462,271,650	496,822,550	671,085,220§	975,136,745‖	1,138,396,158¶	1,529,639,827**

*Including all classes of interest-bearing obligations and all classes of stock. Security issues of steam railways are not included. Compiled from the monthly record of new capital flotations of the *Commercial and Financial Chronicle.*

†Stocks of no par value are entered at a figure representing dollars involved.

‡The detailed reports and summary totals for the year 1922 do not agree. $975,136,745 is here used, since this is the total of monthly reports used. In other tables the total of $930,433,795 for 1922 is used. The latter figure represents a correction of earlier compilations, but the facts necessary for analysis are not supplied for the issue representing this difference.

§Records of security issues for November, 1921, are incomplete. A small volume of known issues on which facts are incomplete have been distributed according to the proportion of the known on which all facts are available among the classes of utilities.

‖Steam utility issues of $6,000,000 and representing .7% of all issues are included in the total.

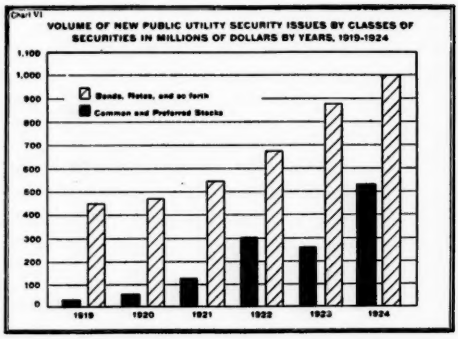
¶Steam utility issues of $300,000 are included in the total.

**Steam utility issues of $2,314,000 and representing about .1% of all issues are included in the total.

the new financing each year. Over the six-year period this class of utilities issued 21% of par value of securities of record issued by all classes of utilities.

A relatively small number of utility corporations supply only gas service. As a result, the proportion of new financing attributable to this class is small, although in 1922 and 1923 this class of utilities accounted for 8% of the total. During the six-year period 5% of the par value of all types of securities issued by all classes of utilities originated with utility corporations doing a gas business exclusively.

Class 3, which includes those corporations that supply gas and electric service, accounts for the largest volume of financing. This combination of services is very common. In 1919, 1921, and 1922 (Table VI) although this class accounted for a smaller proportion of the total issue than did the telephone and telegraph utilities, the exceptional proportions in 1920 (38.6%) and 1924 (35.9%) bring the total for this class above that of any class for the six-year period—28% of the total par value of securities issued.



Those corporations supplying only electric light and power service had a volume of financing second only to Class 3. Thus over the period 1919-1925, financing by this class represented 25% of the total of all classes. When one considers that the single service corporation is not as common as the type rendering two or more classes of service, this proportion becomes all the more significant. Rapid survey of the corporations included in Class 4 (electric) leaves the impression that power companies account for a considerable proportion of this volume.

During the years of smaller total volume of financing (1919, 1920, and 1921) but also in 1922, corporations engaged in the electric railway business and also rendering electric, and in some few instances other than electric, service

TABLE VI. PERCENTAGE DISTRIBUTION OF NEW PUBLIC UTILITY SECURITY ISSUES ACCORDING TO UTILITY CLASS OF ISSUING CORPORATION 1919-1924*

	1919 Percentage of Total	1920 Percentage of Total	1921 Percentage of Total	1922 Percentage of Total	1923 Percentage of Total	1924 Percentage of Total
Telephone and Telegraph	26.8	12.2	29.7	24.9	18.7	17.9
Gas	4.9	2.2	2.2	8.5	8.0	1.6
Gas and Electric	17.4	38.6	24.2	20.7	25.6	35.9
Electric	15.7	25.4	14.1	20.5	32.8	27.6
Railway and Electric	26.6	17.7	25.9	21.1	9.7	8.1
Railway	7.7	2.7	2.7	2.8	2.4	6.8
Water	.9	1.2	1.2	.8	2.8	2.0
All Utilities	100.0	100.0	100.0	100.0†	100.0‡	100.0§

*Including all classes of interest-bearing obligations and all classes of stock. Security issues of steam railways are not included. Compiled from the monthly record of new capital flotations of the *Commercial and Financial Chronicle*.
†Steam utility issues of $6,000,000 and representing .7% of all issues are included in the total.
‡Steam utility issues of $300,000 are included in the total.
§Steam utility issues of $2,314,000 and representing about .1% of all issues are included in the total.

(Class 5) account for a significant proportion of the total of new public utility security issues. In 1923 and 1924, although the volume for this class was over a hundred million dollars par value, it constituted but 9.7% and 8.1% of the total issued. During the six-year period this class of utility corporation supplied 10% of the par value of new security issues of all types.

Corporations rendering electric railway service exclusively (Class 6) did not command any large amount of capital during the period 1919-1925. Although in 1919 this class represented 7.7% of the total and in 1924 6.8%, in the intervening years the percentage did not rise above 2.8. Over the entire six years about 4% of the security issues were by corporations rendering electric railway service exclusively.

Water utility financing (Class 7) was only about 1% of the total over the six-year period. An occasional issue of steam utility securities is recorded but this service is only occasionally rendered exclusively and so is not given separate treatment; the par value involved also is not relatively important.

The proportion of the value of stock issues to total issues of all types of securities varied widely during the six years for the different classes of utilities. Most striking in this connection is the fact that 40.2% of the value of all stock issued during the six years was accounted for by the telephone and telegraph utilities. Class 2 utilities (gas) supplied 7.5%; Class 3 (gas and electric) 19.6%; Class 4 (electric) 29.0%, while the Classes 5 and 6 (railway and electric, and railway) inclusively only 3.2%. Water utilities account for only .5% of the total.

Extent of Holding-Company Financing

During recent years there has been an increasing movement toward consolidation of public utility enterprises. In connection with that development, a considerable amount of financing is necessary which does not necessarily add to the capital invested in the industry. Not infrequently the records of the purpose of a public utility security issue read "to acquire control of." In order to make an approximation as to the

extent of holding-company financing, all the issues of bonds, notes, debentures, and certificates were grouped into three classes on the basis of the character of the issuing corporation. For the purposes of the question here involved, all utility corporations can be classified into three groups: (1) purely holding corporations which do not conduct any operations; (2) purely operating corporations which are not holding securities of corporations which they are not operating; and (3) those companies which are mixed in character, being at the same time operating companies and controlling other operating companies through security ownership. When the ownership of stock by an operating company is the means used to effect consolidation and operation is unified, even though the controlled corporations continue to hold charters or franchises or for other reasons maintain their identity, the unit is treated as an operating company.

On this basis, 62% of the financing during 1924 by the issuance of interest-bearing obligations was by operating companies, 25% by operating companies that also held securities in other public utility corporations, and 13% by purely holding corporations.

Average Yield at Offering Price of All New Public Utility Security Issues 1919-1925

The cost of money to a public utility corporation is an important element in the cost of the service. The experience of the public utility industry in this respect during the last six years and the present trends can be followed by studying the average price which the investor receives for money lent to public utility corporations.

A distinction must be made between the price which the investor receives—the interest yield at the price he paid computed to maturity—and the price paid by the utility corporation. The differential between yield to investor and corporation cost is made up principally of banker's discount, legal expenses, and miscellaneous charges such as for printing and engraving. No attempt is made in this analysis to determine the amount by which the price paid by the corporation exceeds the yield to the investor at offering price. The average yield of all new public utility interest-bearing security issues at the offering price is used to indicate the trend. The true cost to the utility would be some amount above this. The amount of this discount and expense varies with the company, the character of the security, and market conditions. On the average it probably remains relatively constant except during such periods of rapidly rising yields as in 1919 and 1920, when larger discounts are demanded to cover the increased risk.

The present analysis of the trend of the average yield to investors at offering price is based upon a study of 1,308 interest-bearing obligations issued in the United States during the six years, 1919-1924, and the first three months of 1925, representing a total par value of $4,387,290,800, which is 99.2% of all issues of record. Issues of record for which the necessary information as to price of issue was not available and a very limited number of foreign loans for public utility purposes were not included.[4]

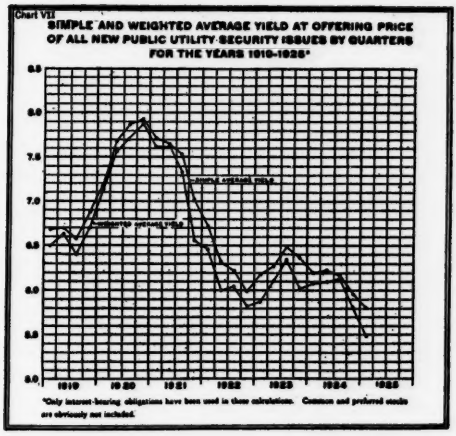
The average yield at offering price reached its highest point during the fourth quarter of 1920. Beginning in

[4] For example, during the first quarter of 1925 two fairly large loans, one Japanese and one German, at the high rate of 7.80% yield were not included.

the third quarter of 1919 there was an uninterrupted rise from a simple average yield of 6.58% on all maturities and classes of interest-bearing securities to 7.94% in the last quarter of 1920 (Table VII). From the first quarter in 1921 through two years to the end of 1922 there was a similarly precipitous and uninterrupted decline from the high of 7.94% to a low of 5.99% (Chart VII). During the first three quarters of 1923 the average yield rose .5%, probably influenced by a greatly increased volume of financing and also by the fact that the lower rates encouraged borrowing by corporations which were unable or unwilling to borrow at the higher rates. Since the last quarter of 1923 through 1924 and the first quarter of 1925, the decline in average yields has been marked but irregular, falling, finally, to a low average of 5.81%.

Both a simple and a weighted average yield are presented so that one may be used as a check on the other. The simple average yield is an average per security issue while the weighted average yield is the yield per dollar. In a period when a large number of small issues (and these are rather generally at higher yields) constitutes but a small portion of the total par value of securities issued, the simple average yield gives too much importance to these small issues. Again, however, when some one issue is exceptionally large, the average yield per dollar of securities issued gives the large issues undue importance. It will be noted that the simple average yield (Chart VII) is consistently above the weighted average yield, indicating that on the average the larger issues were sold at a lower yield to the investor.

An average taken as representative of the level at which public utility



financing occurred may be somewhat misleading. It may happen that a large volume of financing was at rates very much higher than the average and another large volume at materially lower rates, leaving very little at the average rate. The average as computed is not necessarily typical of the rate at which any large volume of securities was issued. The results of a distribution of the volume of bond and note issues only, at quarter percentage intervals, is presented in Chart VIII. In 1919 the range of yields at offering price was between 5.25% and 7.25% with the largest volume between 5.75% and 6%. In 1920, when the highest yields at offering price were reached, the range was from 5.75% to 8.50% with a few scattering issues at even higher rates. In the year 1921 the single average yield on bonds and notes at offering price was 7.45%, but the largest volume was at rates between 6.01% and 6.25%. Similarly in 1922 there was a large volume of financing below 6.34%, the simple average rate for the year. In 1923 the most common rate of issue was between 6.01% and 6.25%, more than twice the volume being issued between those limits than for any other quarter

TABLE VII. WEIGHTED AND SIMPLE AVERAGE YIELD AT OFFERING PRICE OF NEW PUBLIC UTILITY SECURITY ISSUES, 1919-1925*

	ALL MATURITIES†		LONG TERM		SHORT TERM‡	
	Weighted Average Yield	Simple Average Yield	Weighted Average Yield	Simple Average Yield	Weighted Average Yield	Simple Average Yield
The Year 1919	6.55	6.68	6.21	6.25	6.78	7.03
First Quarter	6.49	6.68	6.22	6.21	6.75	7.21
Second Quarter	6.63	6.70	6.29	6.33	6.86	6.99
Third Quarter	6.40	6.58	6.12	6.28	6.54	6.82
Fourth Quarter	6.70	6.78	6.27	6.24	7.20	7.05
The Year 1920	7.55	7.64	7.52	7.59	7.59	7.68
First Quarter	7.14	7.16	6.75	6.64	7.27	7.34
Second Quarter	7.57	7.69	7.40	7.58	7.64	7.72
Third Quarter	7.70	7.87	7.61	7.75	8.21	8.12
Fourth Quarter	7.88	7.94	7.77	7.84	8.15	8.29
The Year 1921	7.13	7.45	7.11	7.40	7.26	7.61
First Quarter	7.62	7.72	7.54	7.61	7.86	7.97
Second Quarter	7.62	7.63	7.58	7.62	8.05	7.65
Third Quarter	7.34	7.53	7.28	7.46	7.90	7.89
Fourth Quarter	6.56	7.02	6.59	7.03	6.35	6.95
The Year 1922	6.06	6.34	6.03	6.32	6.39	6.53
First Quarter	6.46	6.72	6.57	6.75	5.89	6.40
Second Quarter	6.00	6.33	5.98	6.27	6.76	6.96
Third Quarter	6.05	6.23	5.98	6.16	6.80	6.89
Fourth Quarter	5.83	5.99	5.80	6.04	6.60	5.50
The Year 1923	6.04	6.31	5.99	6.26	6.73	6.72
First Quarter	5.88	6.19	5.86	6.17	6.39	6.36
Second Quarter	6.11	6.27	6.02	6.20	6.85	6.65
Third Quarter	6.35	6.49	6.25	6.36	7.16	7.11
Fourth Quarter	6.01	6.36	5.98	6.32	6.52	6.67
The Year 1924	6.03	6.14	6.04	6.16	5.97	6.04
First Quarter	6.08	6.20	6.04	6.20	6.25	6.23
Second Quarter	6.10	6.23	6.15	6.28	5.86	5.94
Third Quarter	6.14	6.16	6.17	6.19	5.72	5.96
Fourth Quarter	5.81	5.96	5.82	5.95	5.78	5.99
The Year 1925	.....	.....	.....	.....	.....	.....
First Quarter	5.49	5.81	5.67	5.82	5.32	5.77

*The yield is computed on offering price to maturity.
†"Short term" includes all maturities of 1-5 years inclusive; "Long term" all issues for longer than five years.
‡Including all classes of interest-bearing obligations, .ei., bonds, notes, debentures, and certificates.

Chart VIII

DISTRIBUTION OF NEW LONG-TERM PUBLIC UTILITY BOND AND NOTE ISSUES ACCORDING TO INTEREST YIELD AT OFFERING PRICE, 1919-1924

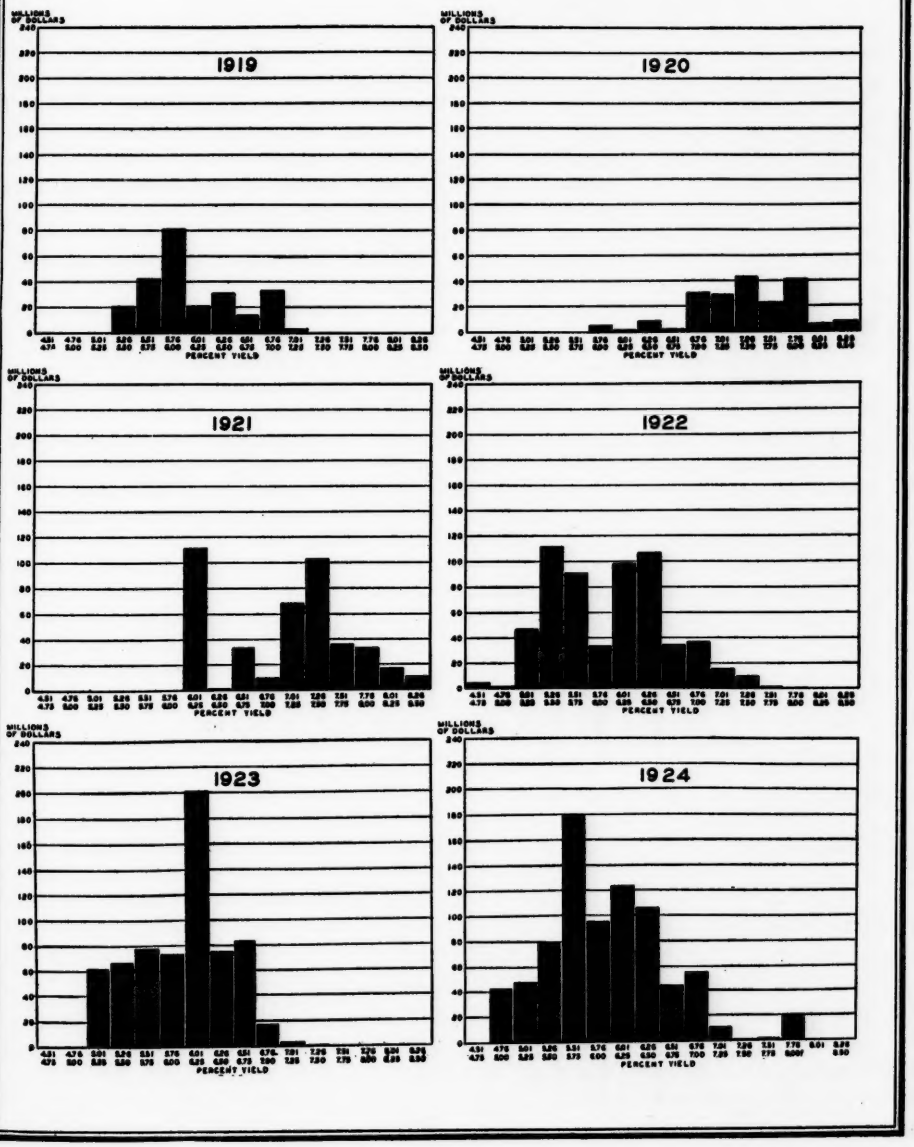


TABLE VIII. WEIGHTED AND SIMPLE AVERAGE YIELD AT OFFERING PRICE OF NEW BOND AND NOTE ISSUES OF PUBLIC UTILITY CORPORATIONS BY QUARTERS, 1919-1924

	Bonds and Notes	
	Weighted Average Yield	Simple Average Yield
The Year 1919	6.54	6.67
First Quarter	6.54	6.68
Second Quarter	6.62	6.69
Third Quarter	6.25	6.52
Fourth Quarter	7.00	6.77
The Year 1920	7.53	7.62
First Quarter	7.09	7.13
Second Quarter	7.56	7.69
Third Quarter	7.67	7.82
Fourth Quarter	7.87	7.94
The Year 1921	7.11	7.45
First Quarter	7.60	7.70
Second Quarter	7.64	7.70
Third Quarter	7.34	7.53
Fourth Quarter	6.55	7.02
The Year 1922	6.03	6.34
First Quarter	6.46	6.76
Second Quarter	5.96	6.30
Third Quarter	6.04	6.25
Fourth Quarter	5.80	5.95
The Year 1923	6.11	6.29
First Quarter	5.84	6.16
Second Quarter	6.22	6.26
Third Quarter	6.34	6.47
Fourth Quarter	6.18	6.34
The Year 1924	5.98	6.12
First Quarter	6.03	6.14
Second Quarter	6.03	6.18
Third Quarter	6.13	6.15
Fourth Quarter	5.76	6.02

percentage interval. For the year 1924, rates of yield between 5.51% and 5.75% were most common, while for the year the simple yield was 6.12% and the weighted yield 5.98% (Table VIII). Comparison of the distribution of the par value of bonds and notes for 1921 with the distribution for 1923 shows the marked change in rates of issue that took place in that two-year period of rapidly falling average yields.

Average Dividend Yield at Offering Price of Preferred Stock

The number of issues of preferred stock increased during the years 1919-1924. In 1919, only seven issues are recorded; in 1920, 13; 1921, 9; in 1922, 35; in 1923, 44; and in 1924, 87 issues of preferred stock are recorded. The average dividend rate at offering price on preferred stock follows the curve for interest obligations rather closely. The simple average yield of 7.16%, in 1919, rose to 7.38% in 1920, and 7.47% in 1921, and then began to fall—to 7.34% in 1922, 7.19% in 1923, and 7.09% in 1924. The weighted average rate began at a higher level in 1919 (7.48%), fell in 1920 to 7.23%, rose to a peak of 7.68% in 1921, and then fell to 7.09%, 6.96%, and 6.93% in the years 1922, 1923, and 1924.

Average Yields by Classes of Utilities

Not all classes of utilities were able to borrow on equal terms during the period 1919 to 1924. In Table IX the simple and weighted average yields at offering price for the various classes of utilities are set forth. The classification is carried further and a segregation according to types of securities is also made. It should be understood that when concerned with a utility class issuing but a small proportion of the total volume, the average rate of yield on the less common types of securities will display little consistency or trend and cannot be depended upon as representing any typical level. Usually the number of issues is inadequate when the classification is carried out in such detail. The

TABLE IX. WEIGHTED AND SIMPLE AVERAGE YIELD AT OFFERING PRICE OF NEW PUBLIC UTILITY SECURITY ISSUES, BY CLASSES OF UTILITIES AND TYPES OF SECURITIES, 1919-1924

	ALL SECURITIES		BONDS		NOTES		DEBENTURES		CERTIFICATES	
	Weighted Average Yield	Simple Average Yield	Weighted Average Yield	Simple Average Yield	Weighted Average Yield	Simple Average Yield	Weighted Average Yield	Simple Average Yield	Weighted Average Yield	Simple Average Yield
1919										
All Utilities	6.55	6.68	6.36	6.38	6.68	7.07	6.37	6.86	7.04	6.72
Electric Light and Power	6.08	6.31	6.00	6.16	6.99	6.90	6.95	6.95	.....	.....
Gas and Electric	6.71	6.82	6.60	6.50	6.89	7.43	7.00	7.00	.....	.....
Railway and Electric	6.98	6.94	6.70	6.67	7.13	7.15	7.00	7.00	7.00	7.00
Gas Utilities	7.28	6.52	6.05	6.14	7.18	6.85	7.00	7.00	.....	.....
Electric Railways	6.96	6.79	6.77	6.65	7.02	6.98	.....	.....	7.04	6.62
Telephone and Telegraph	6.12	6.11	5.73	6.01	6.22	6.23	5.93	5.93	.....	.....
Water Utilities	6.48	6.30	6.00	6.00	7.50	7.50	.....	.....	.....	.....
1920										
All Utilities	7.55	7.64	7.49	7.54	7.57	7.72	7.91	7.90	8.03	7.73
Electric Light and Power	7.58	7.59	7.49	7.45	7.75	7.81	7.82	7.80	.....	.....
Gas and Electric	7.56	7.61	7.53	7.60	7.54	7.57	7.93	7.93	.....	.....
Railway and Electric	7.61	7.82	7.46	7.66	7.68	7.92	8.00	8.00	8.13	7.85
Gas Utilities	6.67	7.37	7.88	7.88	6.53	7.20	.....	.....	.....	.....
Electric Railways	7.97	7.91	7.61	7.82	8.40	8.42	.....	.....	7.93	7.50
Telephone and Telegraph	7.52	7.25	7.45	6.97	7.60	7.67	.....	.....	.....	.....
Water Utilities	6.36	6.85	6.50	7.12	6.34	6.67	.....	.....	.....	.....
1921										
All Utilities	7.13	7.45	7.07	7.37	7.32	7.71	7.65	7.65	6.80	6.92
Electric Light and Power	7.12	7.19	6.94	7.11	9.00	9.00	7.68	7.72	5.50	5.50
Gas and Electric	7.04	7.43	7.05	7.36	6.93	7.51	8.10	8.10	.....	.....
Railway and Electric	7.40	7.58	7.33	7.47	8.02	7.99	.....	.....	.....	.....
Gas Utilities	7.62	7.70	7.74	7.80	7.53	7.45	.....	.....	.....	.....
Electric Railways	7.35	7.53	7.58	7.65	7.05	7.44	.....	.....	7.35	7.62
Telephone and Telegraph	6.69	6.93	6.69	6.93	.....	.....	.....	.....	.....	.....
Water Utilities	7.30	7.33	7.51	7.42	7.20	7.20	7.00	7.00	.....	.....
1922										
All Utilities	6.06	6.34	6.01	6.32	6.31	6.60	6.48	6.65	5.81	5.96
Electric Light and Power	6.02	6.38	5.99	6.29	7.16	7.27	6.00	6.00	7.00	7.00
Gas and Electric	6.10	6.33	6.12	6.39	5.70	5.75	6.30	6.29	.....	.....
Railway and Electric	6.23	6.44	6.16	6.36	6.86	7.09	6.74	6.83	.....	.....
Gas Utilities	6.26	6.33	6.06	6.33	6.84	6.00	7.00	7.00	.....	.....
Electric Railways	6.18	6.22	6.32	6.40	5.65	5.65	7.25	7.25	5.71	5.75
Telephone and Telegraph	5.27	6.10	5.27	6.10	.....	.....	.....	.....	.....	.....
Water Utilities	5.96	5.88	5.96	5.88	.....	.....	.....	.....	.....	.....
1923										
All Utilities	6.04	6.31	6.02	6.26	6.73	6.69	5.95	6.79	5.85	5.89
Electric Light and Power	6.17	6.30	6.14	6.23	6.70	6.80	7.12	7.10	.....	.....
Gas and Electric	6.24	6.35	6.16	6.28	6.74	6.61	6.75	6.84	.....	.....
Railway and Electric	6.37	6.40	6.33	6.32	6.69	6.78	6.50	6.75	.....	.....
Gas Utilities	6.32	6.38	6.06	6.32	7.20	7.20	.....	.....	.....	.....
Electric Railways	6.20	6.29	6.55	6.45	6.37	6.60	.....	.....	5.85	5.89
Telephone and Telegraph	5.44	5.65	5.23	5.65	.....	.....	5.62	5.62	.....	.....
Water Utilities	5.38	5.99	5.33	5.99	6.00	6.00	.....	.....	.....	.....
1924										
All Utilities	6.03	6.14	5.98	6.12	5.97	6.00	6.62	6.70	5.45	5.59
Electric Light and Power	6.00	6.24	5.92	6.18	6.14	6.30	6.80	6.86	.....	.....
Gas and Electric	6.10	6.13	6.03	6.08	6.00	5.96	6.55	6.62	.....	.....
Railway and Electric	6.13	6.14	6.11	6.16	5.65	5.51	6.65	6.66	.....	.....
Gas Utilities	5.74	5.79	5.80	5.73	5.70	5.90	.....	.....	.....	.....
Electric Railways	6.17	6.04	6.25	6.22	5.86	5.56	.....	.....	5.45	5.59
Telephone and Telegraph	5.53	6.12	5.48	6.00	6.55	6.75	6.75	6.75	.....	.....
Water Utilities	5.76	6.09	5.76	6.09	.....	.....	.....	.....	.....	.....

segregation is made not so much to determine the average yields on debentures or certificates but to eliminate these from the mixture of all interest-bearing securities. The trend as represented is influenced by the character of securities included as well as by the more general market changes which are of concern here. Thus, the average rate of all electric railway financing is hardly representative because of the inclusion of equipment trust certificates which can be normally sold at a low yield. For that reason the average yield on bonds issued by electric railways is usually higher than the average yield on all types of securities issued by this class of corporation. Similarly a class of utility corporations which is in a position to issue debentures will appear to be paying a higher rate for new capital than another utility class, although the average yields on bonds issued may be materially lower.

The most useful average yield for comparative purposes is that based on the average yield of bonds. Bonds represent a large proportion of the total for each utility class and by excluding other types of securities a homogeneous base is secured.

Comparing the average yields at which various classes of utilities were financed, few marked or consistent differences are found. The average yield at offering price of telephone and telegraph and water utility securities is lowest in almost every instance. All telephone and telegraph security issues of record during the six-year period were offered at a weighted average yield of 5.99% and all water utility issues at 5.83%. The volume of security issues by water utilities is, however, not comparable to the large volume of financing by telephone and telegraph utilities. "Railway," and "railway and electric" corporation issues were gener-

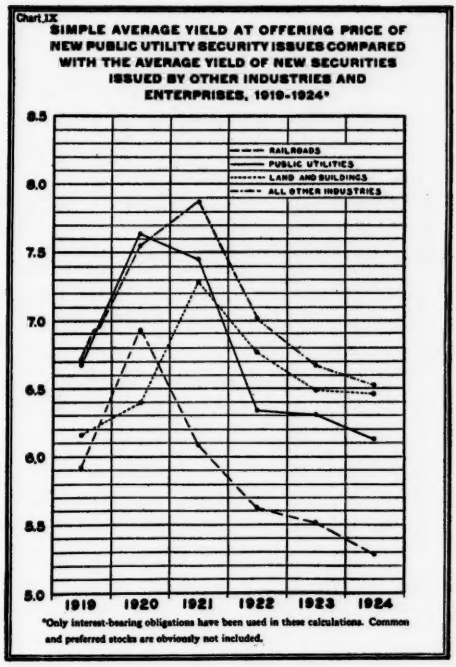
TABLE X. AVERAGE YIELD AT OFFERING PRICE OF NEW PUBLIC UTILITY AND STEAM RAILWAY SECURITY ISSUES COMPARED WITH THE AVERAGE YIELD AT OFFERING PRICE OF THE NEW SECURITY ISSUES OF OTHER INDUSTRIES AND ENTERPRISES, 1919-1924*

Class of Issuing Corporation	1919		1920		1921		1922		1923		1924	
	Simple Average Yield	Number of Issues	Simple Average Yield	Number of Issues	Simple Average Yield	Number of Issues	Simple Average Yield	Number of Issues	Simple Average Yield	Number of Issues	Simple Average Yield	Number of Issues
Iron, Steel, and Copper	6.87	28	7.46	30	7.98	15	6.91	63	6.57	52	6.66	54
Equipment Manufacturing	6.38	8	7.68	14	8.04	7	6.62	2	6.24	9	5.20	12
Motors and Accessories	6.89	11	7.13	10	8.20	8	7.25	16	6.53	13	6.28	8
Other Industrials and Manufacturing	6.57	84	7.58	108	7.85	92	7.08	156	6.73	127	6.62	114
Oil Companies	7.02	22	7.77	29	7.82	36	6.86	22	6.48	25	6.24	21
Land and Buildings	6.16	62	6.40	92	7.29	38	6.77	148	6.49	228	6.46	420
Rubber	7.38	2	7.33	5	8.04	5	6.94	6	7.00	1	6.50	1
Shipping	7.11	14	7.75	21	8.11	8	7.01	11	6.60	6	6.80	4
Miscellaneous	6.61	42	7.40	44	7.80	41	6.95	106	6.74	99	6.57	83
All Non-Utility	6.59	273	7.25	353	7.79	250	6.94	530	6.59	560	6.48	717
All Non-Utility, excluding Land and Buildings	6.72	211	7.55	261	7.88	212	7.01	382	6.67	332	6.52	297
Railways (Steam)	5.92	27	6.94	31	6.09	91	5.63	116	5.51	78	5.29	115
Public Utilities	6.68	123	7.64	156	7.45	152	6.34	226	6.31	256	6.14	331

*Compiled from the monthly record of new capital flotations of the *Commercial and Financial Chronicle*. All types of interest-bearing obligations are included.

ally at the highest average rate of any class. Over the six-year period, the average yield on all types of securities issued by electric railway companies was 6.76% and for "railway and electric" companies 6.50%.

Very little differentiation can be made between the rates at which the "gas," "electric," and the "gas and electric" classes were financed. The average for all securities over the period 1919-1924 for exclusively electric companies is 6.32%, for the gas and electric companies 6.47%, and the exclusively gas companies 6.41%. Differences in the volume of financing, the varying credit of the corporations issuing each security, the type of security selected, the period in which the larger part of the total amount was issued, all obviate any attempt at an array of classes of utilities on the basis of borrowing power further than has been attempted here.



Comparison of Yields on Public Utility Issues with Yields on Other Classes of Issues

The question is asked, How does the rate at which the public utilities borrow capital compare with the rate of other corporations not engaged in a public calling? Such a comparison is presented in Table X and graphically in Chart IX. During 1919, public utilities borrowed at rates just below those paid by all other industries, excluding steam railway and real estate borrowing. In 1920, public utilities paid a higher rate than other industries as a class (Chart IX). Since 1920, however, the improvement has been very rapid for public utilities compared with other industries, until in 1924 only steam railway financing was at lower average rates. During the first quarter of 1925, public utilities borrowed at even lower average rates. Steam railway issues were at a simple average rate of 5.53%, land and building issues at 6.31% and all non-utility industrials at an average rate of 6.22%, while public utilities borrowed the largest volume of any three months' period at an average rate of 5.81%.

The general conclusions that seem justified by the foregoing analysis are: (1) The securities of public utilities are becoming increasingly popular as a form of investment; (2) The investment market has been able to absorb the exceptional volume of utility securities issued in recent years at very favorable rates, both absolutely and comparatively; (3) Consequently there seems to be little reason for general concern over the ability of public service industries as a whole to meet increasing demands for service with a low average cost for the necessary capital.

THE PUBLIC LEASEHOLD SYSTEM IN THE UNITED STATES

By MARY L. SHINE

THOSE who are inclined to "view with alarm" the private receipt of gain from increases in the value of land sometimes express regret over the fact that the United States, which originally held title to so large a part of its lands, failed to keep the title in its possession and retain for the benefit of the whole nation the increments in land value that have accrued. The Belgian economist, De Laveleye, for example, expressed the opinion that we had made a serious mistake in not retaining the land as public property. The United States, starting its career with Europe's experience behind it, at a time when increasing land values were adding to the fortunes of certain great English families, might well, it would seem, have inaugurated a public leasehold system—that is, a system in which the government retains title to the land, and the utilizers pay the rental value into the public treasury—national, state, or local—for the support of the various public services rendered by these governmental units.

Certainly there was, among the founders of the nation, no lack of belief in the tendency of land values to increase. Washington advised investment in lands because "there is scarce a possibility of their falling in price, but almost a moral certainty of their rising exceedingly in value";[1] and the other leaders of the time were agreed with him in this belief in the inevitable increase in land values. Land speculation raged throughout the country, and the speculators entertained great hopes of increasing their fortunes through rising values.

However, no idea of establishing a general public leasehold system for the disposal of the public domain was ever seriously entertained, though Thomas Paine and Alexander Hamilton suggested that the lands be sold with the reservation of quit-rents.[2] Paine seemed to feel that by this system the government might have its cake and eat it, too—"It is by the sale of those lands that the debt may be sunk, without burden to any, and the quit-rent reserved thereon will always lessen, and in time will wholly support the yearly expense of government." Both of these men were, at the time when they made these suggestions, too new to the country to have judged rightly the sense of the people in this matter, and both later recognized that the freehold alone would satisfy the demands of the country.[3]

While the leasehold was never considered as a system for general application, it happened that it did receive a trial in several different cases in our early history, and the results may have some bearing on the question as to what

[1] "George Washington," *Writings,* Edited by Worthington C. Ford, New York, 1889-1893, Vol. VII, p. 214, 14 v.

[2] "Thomas Paine," *Writings,* Edited by M. D. Conway, New York, 1894-1896, Vol. I, pp. 115-116, 4 v; "Alexander Hamilton," *Works,* Edited by H. C. Lodge, New York, 1885-1886, Vol I, pp. 249, 271, 9 v.

[3] "Paine," Vol. I, p. 207; "Hamilton," Vol. III, p. 326.

might have happened if the government had adopted a general leasehold policy.

University Lands

The policy of donating land for the support of schools and institutions for higher education was followed by the Federal Government from the outset of our national career, and, indeed, had its precedents in the Colonial land systems. Though up to 1875 the laws granting land for educational purposes did not specifically restrict the right to sell the land, the states which received the earliest of these gifts were in doubt as to whether they had the right to sell. They construed the gift as constituting a land fund that must be held in public ownership and leased to secure a revenue for the support of universities and schools. This use of the land constitutes a real public leasehold system, and the experiences of the states that tried this system are not without interest.

The earliest of these cases is that of Ohio University. In 1787, when the Ohio Company made its purchase of land from Congress, there were granted to it, for the support of a "literary institution," two townships of land, *to be applied in such manner as the state legislature might direct.* The lands were selected in 1795 — Athens and Alexander townships in Athens County. In 1804 the Ohio University was chartered. The legislature, which, as mentioned above, was to direct the application of the land gift to the use of the university, ordered that the lands be appraised and that the trustees then dispose of them by leases for 90 years, renewable forever, with revaluations 35 years, 60 years, and 90 years from the beginning of the lease, this last revaluation to be final.[4] Rents were to be 6% of the appraised value, and the lands were to be forever exempt from state taxes, but the university was to be allowed to increase the rents by an amount equal to the tax. This virtually gave the state taxes on the lands to the university.

Here we have, it would seem, a very well worked out leasehold system. The revaluation would at intervals transfer to the state the increment in value that might accrue, and the final revaluation after 90 years could be expected to represent a value that would be relatively stable—the rapid increases characteristic of a newly settled country might well be expected to have ended by that time.[5]

If this law had been allowed to stand, the university would have profited greatly through the increased value of the lands and the resulting increase in rents, which according to the terms of the leases were to be 6% on the valuation. But the very next year (1805) a new law was passed identical with the one just described except that it omitted the revaluation clause. The intention of the legislature in this law was clearly to prevent revaluation, but why should it have wished to do this within one year of the passage of the original law? One writer says, "No leases were taken, and much dissatisfaction was manifested. No one could be induced to settle upon and improve the land under

[4] After this final revaluation, readjustments, based on wheat prices, were to be made in the rents at 20-year intervals.

[5] The census gives the average value per acre of lands in Athens County as $19.63 in 1900, $22.08 in 1910, and $28.63 in 1920. If we discount the latter as due to inflation of all land values as a result of the war, it appears that a final valuation 90 years after the taking up of the leases—that is, 1894 and the following years—would not have been an unfair one.

a title that was liable to be disturbed so frequently, especially when land in the adjoining township could be bought outright for $1 an acre or even less. Persons who had been induced to settle upon these lands by those interested in the establishment of the university, were discouraged; many, whose improvements were little, left, while others remained, hoping that some relief would be provided. . . . As nothing could be done under the act, Governor Edward Tiffin, in December, 1804, reported that fact to the legislature and suggested that these lands ought to be valued at a generous price once for all." [6] In opposition to this we have the statement made by Walker, in his *History of Athens County,* that in the year following the passage of the act of 1804, 20,000 acres were applied for by occupants and others. [7] However, Governor Tiffin is reported to have said in his next message that "the settlers on these lands were induced to apply for leases under the impression that the legislature would review the law and be governed by a more liberal policy." [8] The revaluation clause was the feature that was considered illiberal, and in 1805 the law was changed, as has been seen, in accord with the desires of the settlers. The lessees under the new law held perpetual leases at a fixed rental of 6% on the original valuation; all the benefit of increases in value of property then went to them instead of going to the university. [9]

However, the new law had expressly repealed only so much of the law of 1804 as was contrary to it, thus leaving ground for litigation over the question whether the revaluation clauses of the law of 1804, not being expressly repealed but only omitted, still held. In 1841 the revaluation provided for in 1804 was attempted by the university. The lessees appealed to the courts, which supported the university. They then appealed to the legislature, which passed an act saying that the act of 1805 was intended to prevent revaluation. "The pressure brought to bear on the legislature in behalf of the lessees was enormous, though there is no evidence that any but legitimate arguments were used upon the members. The lobby in behalf of the bill is said to have been almost unrivaled in the history of the state." [10]

Because of this action, which unfortunately was perfectly legal, since the original grant had made the disposal of the lands subject to the will of the legislature, revaluation was prevented, and the rent for 44,000 acres of land was $4,200 a year, representing a 6% return on the original value, $70,000. [11]

In 1826 the legislature authorized the sale of the university lands at a price equal to the appraised value at the time of leasing. Only a small amount of land was sold to the lessees at that time, [12] notwithstanding the well-known preference of American people for the freehold. The explanation of this refusal to turn the leasehold into a freehold is found in the privileged position

[6] Peters, W. E., *Ohio Lands,* Athens, Ohio, 1918, pp. 265 ff.

[7] Walker, *History of Athens County,* p. 322, cited by George W. Knight in "History and Management of Land Grants in the Northwest Territory," *American Historical Association Papers,* Vol. I, No. 3, p. 119.

[8] *Ibid.*

[9] Blackmar, Frank W., *Federal and State Aid to Higher Education,* Washington, 1890, p. 217.

[10] Knight, G. W., *American Historical Association Papers,* Vol. I, No. 3, p. 121.

[11] Knight, G. W., and Commons, J. R., *Higher Education in Ohio,* Washington, 1891, pp. 17, 18; Knight, p. 121.

[12] Knight, G. W., *op. cit.,* p. 120.

which the university leaseholders held with reference to taxation. They were, as has been stated above, free from taxation by the state. The university had been given the right to exact from the leaseholders payment of a sum equal to the state taxes, but no attempt to exercise this right was made by the university until 1876. When the university at that late date asserted its claim, it had difficulty with the leaseholders, who, after more than 70 years of freedom from taxation, looked upon that privilege as an established right. The leaseholders appealed to the legislature to prevent the collection of the tax rents, but this time in vain. The taxes, amounting to about $3,000, brought the income of the university from its lands up to $7,200 a year.[13] The policy of the university at present is to sell these leaseholds and deposit the proceeds in the state treasury where they become part of the irreducible debt of the state, the interest going to the university. This fund, when completed by the sale of the remaining leaseholds, will not exceed $65,000. Rents for the lands still held by the university are difficult to collect and they scarcely cover the expenses of collecting them. The additional tax-rents are variable, since they include only the state tax, and change with changes in the state levy.[14]

Ohio University's experience with the public leasehold system was undoubtedly a failure. The original plan showed every intention of establishing a public leasehold system to be applied with as much attention to business principles as is customary in the application of the private leasehold. Why could it not be carried out? Chiefly because the landlord was not an individual or a business corporation but a political group of which the tenants themselves were members. Political pressure exerted by them was too great for their neighbors to withstand, and since the individual interest in the matter of any one of these neighbors was small, the tenants had their way, as they could probably never have had it against a private landlord.

Miami University, in Ohio, has had a somewhat similar experience. In the contract covering John Cleves Symmes' purchase, one township of land was given for the support of a seminary of learning. When Miami University was chartered in 1809, the lands were vested in its trustees by the legislature, which ordered the lands leased to the highest bidders at a valuation of not less than $2 an acre, with rents 6% of the value bid, and revaluation every 15 years.

Here, again, was a system worked out on a business basis, not differing from a private leasehold. But here, also, political pressure of the tenants was too great to make possible the maintenance of the system; for the revaluation clause of the law of 1809 was repealed in 1810 by a legislature in which the majority was composed of the same men who had formed a majority of the legislature which passed the law of 1809. All the university lands were taken up immediately, though the university did not open until 1824.[15] In this case the lands, which are free from state taxes, have remained in leasehold, and the rents paid for them are less than the state taxes on the true value of the lands would be.[16] As a result, the uni-

[13] Knight and Commons, pp. 17, 18.

[14] Information given by an official of the university.

[15] Knight, pp. 122-124; Blackmar, pp. 218, 219.

[16] Personal letter of one of the trustees. The average value of the land in Butler County, in which Oxford Township is situated, was, in 1919, nearly $100 an acre; so that the real value on which this income was received was probably more than $2,000,000.

TABLE I. EXPERIENCE OF FOUR OTHER STATES WITH THE LEASEHOLD SYSTEM

State	Institution	Date of Grant	Date Leasing Ordered	Date Sale Ordered	REMARKS
Indiana.....	Vincennes University.....	1804	1807	1807 (4,000 acres only)..... 1822.....	Earliest instance of abandonment of the leasing policy*
Indiana.....	Indiana University.	1816	1822	1827.....	Lands sold early and at a sacrifice.†
Illinois.....	State Normal University..... Southern Illinois Normal University.....	1804 1818	1821	1829 (legislature ordered sale) 1831 (Congress authorized sale).....	Lands ordered leased in 1821 were said to be valueless; no leases were taken. When substitute lands were given, they were sold.‡
Mississippi...	Jefferson College...	1803	1812	1832.....	Leases for 99 years. Few were taken because of competition of federal land. After 1820, lessees threw over their lands though trustees offered to abate one-half of amounts due.§
Mississippi...	University of Mississippi.....	1819	1819	1833.....	Leases for not more than four years given; little return from these, and lands reported in 1833 to be deteriorating—sale ordered 1833.‖
Alabama.....	University of Alabama.....	1818 1819	1819 1822	1821.....	See footnote ¶.

* Woodburn, James A., *Higher Education in Indiana*, Washington, 1891, pp. 29 ff; Knight, *Land Grants*, pp. 124 ff.
† Woodburn, pp. 80 ff.
‡ Knight, p. 132; Blackmar, pp. 231 ff.
§ Mayes, E. L., *History of Education in Mississippi*, Washington, 1899, pp. 28, 29.
‖ *Ibid.*, pp. 119 ff; Blackmar, p. 268.
¶ The law of 1822 permitted purchases on credit to be turned into perpetual leaseholds, and many purchasers took advantage of this. The university officials neglected, for the most part, the collection of the rentals; and in 1869 the ledger containing the record of the leaseholds was mutilated by a student (acting as quartermaster in the president's office) who tore out the pages on which they were listed. Thereafter it was impossible to determine which of the original lands still belonged to the university as leaseholds. (Willis G. Clark, *History of Education in Alabama*, Washington, 1889, pp. 32, 33).

versity receives about $6,500 a year from the university township.[17]

The experience of some other states to whose "seminary lands" the leasehold system was at first applied are given in Table I, above.

In a number of other cases university lands were leased for short terms during the territorial period and were sold as soon as statehood gave full title to the lands, or (after 1875) when they could be sold at the minimum price fixed by Congress in its donation of university lands. These temporary leases, however, do not fall under our definition of the leasehold system. Neither do the leases given at present by western universities for lands which they have not been able to sell. Even in these cases, however, the rents are sometimes difficult to collect,[18] and yield a very small revenue.[19] The leases of mineral lands belonging to the University of Minnesota are of a somewhat different character and will be considered later.

School Lands

When the leasehold system was applied to lands given by the Federal Government for the support of common schools, there was the same failure to maintain the application of the business principles of the leasing system that occurred in the case of the university lands.

In 1803 Ohio received from the Federal Government section 16 in every

[17] Catalog 1919-1920, p. 9. *The Miami University Financial Report for Year Ending June 30, 1920,* (Miami University Bulletin, Series XVIII, No. 11, Oxford, Ohio, 1920) reports an income of $6,955.56 from 23,403 acres of land, which would include several hundred acres in addition to the university township.

[18] Lane, J. J., *History of Education in Texas,* Washington, 1903, p. 188.

[19] *Ibid.*, pp. 136, 137; *Catalog* of University of Arizona, 1923-1924, p. 23; *Catalog* of University of New Mexico, 1917.

township, or lands equivalent thereto, for the support of schools in these townships. The legislature ordered the leasing of these lands for terms of 7 to 15 years, the rents to be paid in improvement instead of money. Few of these improvement leases were taken up, for the settlers preferred buying land on credit from the government. In 1803 a system of money rents was authorized with leases for not more than 15 years, on the best terms obtainable.

In 1809 a law was passed permitting school lands in that part of Ohio known as the Virginia Military Reservation to be granted in perpetual leases at a rent equal to 6% of the price bid. The lease could not be altered in favor of the state but might be changed in favor of the lessee. "As a result of these laws there are today under lease about 10,000 acres in this district at an annual rent of 12 cents an acre. In 1810 the governor expressed a mild doubt whether these laws were beneficial to the interests of the schools. Not till many years later, however, did any general opinion arise that such legislation was unwise." [20] In 1816 the legislature repealed these laws and ordered leasing to the highest bidder for 99 years with revaluation in 1835 and every 20 years thereafter.

In 1817 a modification of the law that had been passed in 1816 for the Virginia Military District was applied to the school lands of the whole state. It allowed leasing for 99 years at an appraised valuation, with revaluation every 33 years. There was much discontent with this and much special legislation concerning these lands at the instigation of the lessees. [21] This legislation favoring certain persons, many of whom were related to the legislators, [22] was a source of scandal and of great loss to the state, both because of loss of income from the land and because of the expense of legislative sessions which were largely devoted to the passing of these special laws. [23]

The scandal had become so great that in 1821 a commission was appointed to investigate, and as a result of its findings a senatorial committee charged fraud, undervaluation, and squandering of the proceeds. It said that nothing could be done under the lease system, and urged that all lease laws be suspended and that lessees be allowed to surrender their leases. This was done, and Congress in 1826 gave permission to sell. In 1827 lessees were permitted to buy their lands at the last valuation, which gave them the benefit of from 3 to 10 years' increment in value. [24]

The memorial to Congress asking for permission to sell the lands stated as objections to the leasing system: (1) Only persons wholly destitute would lease land while facilities for purchase were so great; (2) superintendence of the leased lands was inadequate but expensive; (3) timber was being wasted by the cutting done by lessees; (4) the system made for the existence of an undesirable tenant class in Ohio. [25]

One writer has said, concerning Ohio's experience with the leasehold system: "It was another demonstration that land ownership is the best basis of social and economic contentment and

[20] Knight, pp. 45, 46.

[21] *Ibid.*

[22] Atwater, Caleb, *History of Ohio*, Cincinnati, 1838, pp. 253 ff; Knight, p. 49.

[23] Randall, E. O., and Ryan, D. G., *History of Ohio: Rise and Progress of an American State*, New York, 1912-1915, Vol. III, p. 173; Knight, pp. 43 ff; Atwater, pp. 253 ff.

[24] Knight, p. 54; *cf.* Atwater, p. 400.

[25] *American State Papers, Public Lands*, Vol. IV, p. 49.

stability of government. Even the legislature, in 1824, when appealing to Congress for permission to sell these lands, was constrained to say 'that the great body of those who constitute the strength and basis of every government, and who are to be considered as the friends of good order and public improvement, are among those who are the owners as well as the occupiers of the soil'." [26]

The legislature further declared that the evils they were seeking to escape "arise wholly from the system of granting these lands upon leases, and are such as cannot be remedied by any course of legislation whatever, if, as some have supposed, the state has not the power under the term of the original grant of disposing of these lands in fee." [27]

Indiana, at the time of its entrance into the Union in 1816, inaugurated a leasehold system for its school lands, titles to which were in this case in the townships instead of in the state at large. No sales were to be permitted before 1820, but leases for 7 years were to be issued. In 1821 a special committee investigated the subject and recommended the sale of the lands, pointing to the experience of Ohio as a reason for abandoning the leasehold system. However, as no permission had been granted by Congress for the sale, the state, in 1824, authorized the disposal of the lands on the best terms obtainable by anything except sale in fee. All the worst evils of the leasehold system were permitted by this law, but fortunately, the legislature, in 1825, forbade the issuance of further leases for terms greater than 10 years, and in 1828 Congress gave the desired permission to sell if the townships consented. A small part of this land, scattered among a number of counties, remained unsold. [28]

Illinois was granted its school lands when it became a state in 1819 and adopted the policy of leasing them for 10-year terms. In 1829 the legislature decided to sell the lands as soon as permission to do so was obtained from Congress, and in 1831 the sale began without that permission. The reasons given were that the children of that generation would derive no benefit unless the lands were sold, and that the lands were being stripped of timber by lessees. Considering the fact that most of the sections were prairie lands without timber, the second reason seems absurd. [29] Governor Ford believed that the real reason for abandoning the leasehold was the desire to please the lessees, who wished to purchase at low prices the lands which they were occupying. He said, "I speak what I know when I say that the laws to sell school lands were passed to please the people who were settled upon them who wished to purchase them at Congress price, while the other inhabitants, being divided into little factions and thinking more of success at one election than the interest of all posterity and acting upon the principle that what is everybody's business is nobody's business, aided or suffered the mischief to be done." [30]

Table II, on the following page, shows other cases of attempts to establish the leasehold system for school lands.

Many western states are leasing, chiefly for grazing purposes, their un-

[26] Peters, *Ohio Lands*, pp. 351 ff. Statement of legislature quoted from *22 Laws of Ohio, Local 153*.

[27] *American State Papers, Public Lands*, Vol. IV, p. 49.

[28] Knight, pp. 64 ff; Woodburn, p. 58.

[29] Knight, p. 79.

[30] *Ibid.*, p. 80, note, quoting Ford, *History of Illinois*, p. 79.

TABLE II. OTHER STATES WHICH HAVE ATTEMPTED TO ESTABLISH THE LEASEHOLD SYSTEM FOR SCHOOL LANDS

State	Leasing Begun	Sales Begun	REMARKS
Tennessee..	1806	1825	Much loss. Resistance of squatters on lands to sale.*
Mississippi	1818	Some before 1833	Leased on sale basis—no rents—only taxes. Often unpaid.†
Arkansas..	1829	1843	Congress authorized sale 1837.‡ State ordered sale 1843.§
Florida....	1839	1848	Intention was not to sell but to lease lands for benefit of each township; only one township took advantage of this. Consolidation and sale from 1848.‖

*Swift, Fletcher H., *A History of Permanent Common School Funds in the United States, 1795–1905*, New York, 1911, pp. 394–398.
†*Ibid.*, pp. 325–327; and reports of officials in answer to questionnaires.
‡Shinn, J. H., *History of Education in Arkansas*, Washington, 1900, pp. 11–16.
§*Cyclopedia of Education* (Monroe), article on Arkansas.
‖Bush, George Cary, *History of Education in Florida*, Washington, 1889, p. 15.

sold school lands; but, as in the case of the university land of these states, this renting system is only a temporary expedient and not a real leasehold system.

Saline Lands

In 1781 Pelatiah Webster proposed that "all salt licks and mines, and all valuable fossils in which this country greatly abounds, may be reserved and sequestered for public use. A great revenue may grow out of them; and it seems unreasonable that those vast sources of wealth should be engrossed and monopolized by any individuals. I think they ought to be improved to the best public advantage, but in such manner, that the vast profits issuing from them should flow into the public treasury, and thereby inure to the equal advantage of the whole community." [31] Three years later Washington inquired whether there would be any impropriety in reserving for special sale mines, minerals, and salt springs, so that the public instead of "the few knowing ones" might receive the benefits. . . . "without infringing any rule of justice." [32]

In the ordinance of 1785 the reservation of salt springs was not included, though it had been suggested, [33] but in 1796 Congress passed an act providing for the reservation of salt springs and an area equal to one square mile about them for the use of the United States. The act of 1800 gave the surveyor-general the right to lease these lands; but with the beginning of the admission of new states the policy of giving "salines" to the states was inaugurated, and was followed up to the time of the admission of Nevada. [34]

Up to 1820 Congress absolutely prohibited the sale of salt-spring lands by the states to which they were given;

[31] Webster, Pelatiah, *Political Essays on the Nature and Operation of Money, etc.*, Philadelphia, 1791, p. 49.

[32] "George Washington," *Writings*, Edited by Worthington C. Ford, Vol. X, pp. 428-429.

[33] King, Rufus, *Life and Correspondence*, Edited by C. R. King, New York, 1894-1900, Vol. I, pp. 91-92.

[34] Donaldson, Thomas. *The Public Domain*, Washington, 1883, p. 217.

from 1820 to 1845 the prohibition might be lifted by special consent of Congress; from 1846 to 1875 (when the system of giving salines to the states was abandoned) there was no restriction on the sale. During the period when sales were prohibited or restricted, the leasing system was used, and Congress tried to maintain control over this leasing. Up to 1820, states were not permitted to lease the salines for more than 10-year periods. States admitted between 1820 and 1846 were permitted to give leases for longer periods, if they obtained the consent of Congress. After 1846 the states were given a free hand in disposing of the lands by either lease or sale.[35] In this case 26 years were needed after the first break in the leasehold system to bring about its fall.

Mineral Lands

The abandonment of the policy of leasing salt springs imposed on the states by Congress coincides with the abandonment of a similar policy which Congress had been using for its reserved mineral lands. Arguments in favor of reserving salt springs, mines, and mineral lands, which have already been touched upon, and which did not bring about the reservation of salines in the Ordinance of 1785, did succeed in getting into that ordinance a clause reserving "one-third part of all gold, silver, lead, and copper mines to be sold, or otherwise disposed of as Congress shall hereafter direct," but left in doubt the policy of the government in relation to holding, leasing, or selling mines or mineral lands. In 1807, however, Congress, in an act for the sale of certain lands in Ohio and Indiana, inaugurated a policy of leasing mineral lands. This policy was maintained[36] until 1846, when a law was passed inaugurating a system of sales of mineral lands.

The abandonment in 1846 of the leasing system for mineral lands occurred only after it had been considered for some years. As early as 1839 the House of Representatives had passed a resolution asking the President[37] "to cause to be prepared a plan for the disposal of the public mineral lands, having reference as well to the amount of revenue to be derived from them and their value as public property, as to the equitable claims of individuals upon them." The system was not changed, however, until Polk's administration. In his first annual message Polk, with characteristic vigor, attacked the whole system. "The present system of managing the mineral lands of the United States is believed to be radically defective. More than a million acres of the public lands, supposed to contain lead and other minerals, have been reserved from sale, and numerous leases upon them have been granted to individuals upon a stipulated rent. The system of granting leases has proved to be not only unprofitable to the government, but unsatisfactory to the citizens who have gone upon the lands, and must, if continued, lay the foundation of much future difficulty between the government and the lessees. According to the official records, the amount of rents received by the government for the years 1841, 1842, 1843, and 1844, was $6,354.74, while the expenses of the system during the same period, including salaries of the superintendents, agents, clerks, and incidental expenses,

[35] Orfield, M. N., "Federal Land Grants to the States, with Special Reference to Minnesota," *University of Minnesota Studies in Social Sciences*, 1915, No. 2, p. 71.

[36] The mineral lands of Missouri were permitted to be sold by an act of Congress approved March 3, 1829.

[37] Van Buren.

were $26,111.11, the income being less than one-fourth of the expense. To this pecuniary loss may be added the injury sustained by the public in consequence of the destruction of timber, and the careless and wasteful manner of working the mines. The system has given rise to much litigation between the United States and individual citizens, producing irritation and excitement in the mineral region, and involving the government in heavy additional expenditures. It is believed that similar losses and embarrassments will continue to occur while the present system of leasing these lands remains unchanged."[38]

This straightforward denunciation of the system was followed by immediate results, and the policy of selling mineral lands outright was inaugurated by an act approved July 11, 1846, which provided for the sale of reserved lead mines and contiguous lands in Illinois, Arkansas, Iowa, and Wisconsin.

When the question of the disposal of mineral lands in California, Utah, and New Mexico came up later, and the suggestion that they be leased was again considered, President Fillmore, in his message of December 2, 1849, said: "The mineral lands of California will, of course, form an exception to any general system which may be adopted. Various methods of disposing of them have been suggested. I was at first inclined to favor the system of leasing, as it seemed to promise the largest revenue to the government and to afford the best security against monopolies, but further reflection and our experience in leasing the lead mines and selling lands upon credit have brought my mind to the conclusion that there would be great difficulty in collecting the rents, and that the relation of debtor and creditor between the citizens and government would be attended with many mischievous consequences." [39] Apparently the leasehold system had proved as unsatisfactory for the salt springs and the mineral lands as it had for agricultural lands in the new country opened up.

The leasehold system was simply not acceptable to settlers in the conditions that existed when the land was being taken up. "One of the most remarkable circumstances in our colonial history is the almost total absence of leasehold estates. * * * In fact, partly from the cheapness of the land and partly from innate love of independence, few agricultural estates in the whole country have at any time been held in lease for a stipulated rent." [40] "* * * One great reason for people (the better sort especially) leaving their native country, was to avoid the dependence of landlords, and to enjoy lands in fee to descend to their posterity that their children may reap the benefit of their labor and industry." [41]

Other Tenures Short of Full Ownership

I. Quit-Rent System

Evidence that nothing short of allodial tenures would have succeeded in the settlement of the United States is also found in the record of the quit-rent system of colonial days. The English quit-rent, a small sum paid by the tenant on a manor to be freed from, or "quit of," the services due from his holding, was introduced into the American col-

[38] Donaldson, *op. cit.*, pp. 307, 308.

[39] *Ibid.*, pp. 307-309.

[40] *Ibid.*, p. 466.

[41] Report of Cadwallader Colden, Surveyor-General, on "The State of the Lands in the Province of New York, in 1732" in *Documentary History of the State of New York*, Edited by E. B. O'Callaghan, Albany, 1849-1851, (4 v.) Vol. I, p. 384.

onies by the proprietors. They sold the land for a purchase price, reserving the right to collect a quit-rent, which varied in amount at different times and in different colonies, but was most often, perhaps, two shillings for a hundred acres. When proprietary colonies became crown colonies, the quit-rents became payable to the crown, and resembled, in that feature, the public leasehold system. The records show that, in general, both proprietary and royal governments failed to make a success of the quit-rent system, Maryland being a notable exception in this matter.

"The total amounts received from the quit-rents were often considerable. * * * But the sums were always affected by the refusal of the colonists to pay, by the difficulties of collection, and by the large outstanding arrears that everywhere accumulated. The proprietors of the soil in New Hampshire and the Jerseys had almost nothing to show for their titles, and the crown in New York netted very meager returns from the quit-rents of that province. Taking the British colonies as a whole, there were many instances in which the system worked so badly that the obligation to pay remained little more than a dead letter." [42] Winthrop said, in 1698, that the people had a "strange notion and fright of the word quit-rent." [43]

The situation in New York was a particularly bad one—so much so that the settlement of the state was retarded because settlers deliberately avoided it on account of its bad land system. Quit-rents at varying rates were due to the Dutch patroons whose titles were recognized by the British Crown, as well as to the Duke of York, and, later, to the Crown. Sheriffs refused the duty of collecting quit-rents, which might cost them their lives; and large arrears accumulated. Many persons acknowledged that they had no idea of paying their quit-rents, and others openly bragged that no New York jury would award a verdict for the Crown in a suit of arrears. [44] Burnet, who was governor of the colony from 1720 to 1728, secured decrees for the collection of arrears of quit-rents due to the Crown, but "so strong was the outcry that Burnet's successor, Montgomerie, was reported to have refused either to hold the court or to concern himself with the quit-rents." Governor Cosby tried to enforce the collection in 1732, but the judges took the popular side. Attempts to secure an act of the assembly for enforcement were defeated by landholders in general and especially by the holders of large estates.[45] In 1761 out of a rent roll of £1,806 only £800 were collected, and the accumulated arrears amounted to £18,888.[46]

Strangely enough, after the experience in colonial times, the state did not abolish the quit-rent system at the time of the break with Great Britain, though it offered commutation of quit-rents due to the state to all landholders that desired it and remitted all arrears that had accumulated up to 1783. It continued to appropriate for certain purposes the quit-rents receivable by the state, but probably these grants were never paid. The state quit-rents were abolished by the constitution of 1846.[47]

[42] Charles M. Andrews, in introduction to *Quit-Rent System in the American Colonies*, by Beverly Bond, New Haven, 1918, p. 18.

[43] Bond, p. 40.

[44] *Ibid.*, 254-266.

[45] *Ibid.*, 266-270.

[46] *Ibid.*, 270-279.

[47] Bond, pp. 283-284. The quit-rents that caused the "Anti-Rent War" in 1839 and the following years were due to private owners. A full account of this interesting episode in the history of the state of New York is found in E. P. Cheyney's *The Anti-Rent Agitation in the State of New York*, Philadelphia, 188?.

II. Credit System for Land Sales

So strong has been the feeling that full ownership was the right of every cultivator of the lands, that even the deferred ownership involved in the credit system (in use from 1800 to 1820) for the sale of public lands was unsatisfactory. The government did not enforce the contracts, which provided for the relinquishment of land and its resale when the payments were not made. No one dared to buy the land held by the defaulting purchaser, and Congress passed a long series of Relief Acts, 1806 to 1832, extending time of payment, remitting interest, allowing relinquishment of the part unpaid for and retention of an amount of land covered by payments already made.[48]

It is possible that a somewhat similar situation will arise in the West, where today settlers are being sold lands with shares in the government-constructed irrigation system on deferred payments. Arrears of payments are shown in most of the accounts,[49] and men who have been concerned in the construction of these projects are not at all sanguine concerning the possibility of securing full payment from the landholders.

Present-Day Public Leaseholds

The public leasehold system which failed in these cases when new land was being opened up appears to work much better where land has already attained a high and relatively stable value, although the advantages to be gained from it cannot be so great at this time. The state of Minnesota, for example, derives a considerable income from leases of its mineral lands and royalties paid by those exploiting these lands.[50]

A few lots out of the Illinois school land grant have been saved and are still owned by the city of Chicago. When Chicago was incorporated in 1833, its voters petitioned for the sale of school lands, and all of these were sold[51] except four blocks, title to which was vested in 1839 in the city of Chicago, which ordered the lands to be leased. Later, sales were authorized; but much of this land, in the heart of Chicago, is still under lease and gives a considerable income to the Chicago schools.[52] The maintenance of these leaseholds as good income-producing property is not without its difficulties, however, for each periodical revaluation and increase of rents is resisted by the lessees, who raise objections and sometimes resort to litigation.[53] This resistance is not entirely unreasonable, for the Board of Education waived its right of revaluation in some leases, holders of which pay certain fixed rentals throughout the duration of the lease, an arrangement which results inevitably in discontent among the holders of leases that require reappraisal at intervals. At present no leases are being made without provision for revaluation, and though the appraisal value was nearly doubled[54] the revalua-

[48] Treat, Payson J., *The National Land System*, 1785-1820, New York, 1910, pp. 127, 143, 161.

[49] *Federal Reclamation by Irrigation*, Senate Executive Document 92, 68th Congress, 1st Session (1924) p. 211. The account to 1923 shows that $126,194,163 of the original construction costs are still unpaid, while arrears on maintenance charges and water rentals amounted to $5,868,624.99.

[50] Orfield, p. 228.

[51] The total price was $36,619.47. Paul Monroe, *Cyclopaedia of Education*, New York, 1911-1913, article, "Chicago."

[52] *Comptroller's Report*, 1922.

[53] Currey, J. S., *Chicago: Its History and Its Builders*, 1912, Vol. III, p. 290, 5 v; M. R. Maltbie, "Municipal Functions," *Municipal Affairs*, Vol. II, p. 579.

[54] *Chicago Realtor*, May, 1925, Vol. XXXVIII, No. 5, p. 11.

tions of 1925 went through apparently without difficulty.

The city of St. Louis also retains some of the land given by act of Congress of June 13, 1812, to towns and villages in Missouri for the support of schools. This is leased for 10-year periods with the privilege of 2 or 3 renewals of 10 years each. The lessees pay 6% on the appraised value and taxes.[55] The school board has very little trouble with the collection of rents or with reappraisals. It the lessee wishes to purchase, he may do so, but only at public auction, and at a price not less than 50% more than the appraised value.

Certain other municipalities derive considerable incomes from ground rents of publicly owned sites of high value.

A questionnaire that was sent to cities and states whose financial statistics showed more than $1,000 income from rentals of real estate, while not entirely satisfactory either in the number of returns it brought or in the amount of real information elicited, seemed to bring out the fact that, even from the public, people do not expect to get the use of valuable property for nothing. Nor would an effort to get it for little or nothing receive the support of popular opinion as it did in the pioneer days when land was less valuable and when ownership was general. The resistance to revaluation reported in a few cases gives evidence that they do desire to get it for as little as possible, and it is probable that their efforts to beat down the cost are more successful, directed as they are against an impersonal government, than they would be if directed against the active self-interest of a private owner of property.

Desirability of Public Leasehold?

The cases that have been considered cannot be brought forward as furnishing proof that the leasehold system, if generally applied, would have failed, because they are all complicated by the fact that they existed side by side with a system of outright ownership. It might be argued that the competition of the government sale of cheap land was the sole reason for the failure of the leasehold in these cases. Perhaps such an argument is sound; certainly it cannot be disproved by the evidence collected here.

Is not the more fundamental cause to be found, however, in the fact that governments under popular control are subject to pressure upon the legislatures to bring about conditions desired by their citizens? The government acting as a landlord is a weak defender of its interests in comparison with the private landlord. No individual of those in control has any large personal interest at stake, and to defend the public's interests against the pressure brought to bear by tenants who are friends and fellow citizens as well as voters is more than can be expected of the legislator.

That this pressure would have been exerted even if a general public leasehold policy had been inaugurated seems unquestionable, for no other tenure than outright ownership would have satisfied the great mass of the people. It was what they had come to seek in this country. "Land hunger was the master passion which brought the men of the seventeenth and eighteenth centuries across the sea and lured them on to the frontier. Where hundreds sought for free-

[55] *Report of Board of Education of St. Louis*, 1916-1917; Walter B. Stevens, *History of St. Louis*, 1911, pp. 614, 617; Marshall Snow, "The City Government of St. Louis," *Johns Hopkins University Studies*, 1887; Maltbie, in *Municipal Affairs*, December, 1898, Vol. II, p. 579.

dom of worship and release from political oppression, thousands saw in the great unoccupied lands of the New World a chance to make a living and to escape from their landlords at home. To obtain a freehold in America was, as Thomas Hutchinson once wrote of New England, the 'ruling purpose' which sent colonial sons with their cattle and belongings to some distant frontier township, where they could thrust back the wilderness and create a new community." [56]

There may be some consolation, however, to those who regret our failure to hold our lands in public ownership, in the question that has been raised: Would the rents yielded by a general public leasehold system be much greater than the taxes under the existing system? Certainly they would be greater in a boom year such as the year 1919 was. In that year six counties in six different states were studied and the taxes ranged from 15% to 66% of the net rents before deducting taxes. [57] Even if the net rents were somewhat less in a general leasehold system, they would probably still be considerably more than taxes in such a year. But what of years of depression? Would not the government maintaining a leasehold system find itself with leases thrown back on its hands, unable to dispose of them, and drawing no income from them? Would not such losses go far to offset the gains of the prosperous years?

When we think of things as they are, we are apt to concentrate on the difficulties that attend them and the faults and inadequacy of the system. When we think of the things that might have been, we see them working out perfectly according to theory and plan. May it not be that the advantages which we seem to have missed in failing to establish the public leasehold system are more or less illusory, after all?

[56] Andrews, Charles M., *Colonial Folkways;* Yale University Press, 1919, chap. ii.

[57] Figures taken from a table prepared by C. O. Brannen of the Bureau of Agricultural Economics, U. S. Department of Agriculture.

RELATIONSHIPS OF LANDLORDS TO FARM TENANTS

By F. A. BUECHEL

POPULAR thought on the tenancy problem in the United States has long cultivated the feeling that tenancy is a mark of subserviency and that this is contradictory to our ideal of a free, land-owning people. The tradition is that the best results from an economic point of view are obtained by full and free private ownership of the land. Tenancy as a departure from this ideal has popularly been supposed to violate the cardinal American declaration of faith that "all men are created free and equal." The relationships of landlord and tenant have been felt to be akin to the master and slave or lord and serf relations, which are in keeping with a medieval economic system rather than the modern economy of free competitive enterprise. A natural conclusion from this point of view is that nothing good or wholesome can come out of landlord and tenant relationships, and that the only remedy is to abolish tenancy.

For some years, however, this attitude toward tenancy has been changing. Instead of regarding the tenancy system as foreign to our fundamental economic institutions, many people have come to recognize that tenancy has a legitimate place in our economic order. Coincidently, the relationships of landlord and tenant are being carefully examined to cull the bad practices from the good in order to promote better relationships.

Yet some people still "view with alarm" our "rapid increase" in tenancy, and attribute to tenancy most of the ills, social and economic, which manifest themselves in rural communities. Since this view is widely held and expressed, it may repay us to summarize briefly the present status of tenancy before considering the desirability of some outstanding features of landlord-tenant relationships.

Present Status of Tenancy

Tenant-operated farms increased from 25.6% of the total in the United States in 1880 to 35.3% of the total in 1900, and from 35.3% in 1900 to 38.1% in 1920. In other words, the relative increase in tenancy was three and one-half times as great in the former period as it was in the latter. As a matter of fact, we are probably close to a stationary stage so far as the relative increase in tenancy is concerned, and many of the evils now imputed to the institution of tenancy would remain unchanged if tenancy were abolished overnight.

Moreover, tenancy statistics lose much of their harshness when it is considered that 23% of the tenants are relatives of the owners; another 23% are "croppers" who would otherwise, in the main, be common laborers; and another 10% are themselves land owners.[1] A large proportion of tenants not included in these three categories are probably making progress toward the ownership goal. If other factors are favorable, landlord-tenant relations can be made almost ideal because of the proximity of landlords to their farms.

[1] *1923 Yearbook*, United States Department of Agriculture, pp. 510, 527, 568.

Whereas 78.8% of the landlords lived in the counties in which their farms were located according to the census of 1900, in 1920, according to a special study of 275,000 farms,[2] 80% lived in the county where their farms were located, 11% in the adjoining county, and only 9% at a greater distance.

That tenancy is an effective way to rise to ownership is indicated by the fact that between 1915 and 1920, of all farmers who attained farm ownership in the cotton, corn, and wheat belts, from 60% to 80% of them reached it by the "tenancy route."

The foregoing statements are not designed to minimize the seriousness of our tenancy problems, but to suggest that the "shortcomings of tenancy may be charged against tenancy under the present landlord-tenant relationship rather than against any essential feature of tenancy"[3] as such. "In the discussion of farm tenure it is usually assumed that the only alternative is between farm tenancy and farm ownership. As a matter of fact, the real alternative is, in very many cases, between farm tenancy and working on a farm for wages. If the renting of farms were prohibited on and after July 1, 1927, by an amendment to the Federal Constitution, then a large fraction of the two and one-half million farm tenants now in the United States would become not farm owners, but farm laborers."[4]

A Good Leasing System Necessary

Instead of looking upon tenancy as something abnormal—an evil to be eradicated at the earliest possible moment—we should regard it as a necessary institution in the agricultural industry, at least under certain conditions and places, capable of rendering effective service in assisting competent, but landless, men to become owners of farms.

The problem then becomes one of making a leasing arrangement in accordance with economic principles. This is all the more imperative because of the fact that the highest percentage of tenancy is generally associated with the most productive land. Because certain land is highly productive, it attains a high value; and because of its high value, young men just beginning their productive careers are unable to purchase it outright; they must, therefore, purchase its annual use under some sort of leasing arrangement.

Not only do young men just starting out in the farming business ordinarily find themselves unable to purchase high-priced land, but also they frequently possess insufficient funds properly to equip such a farm with the amount and quality of equipment, work animals, and productive live stock which should be associated with high-quality land.

The most economical use of high-priced land requires that the quality and quantity of labor and capital applied to it must correspond to the quality of the land used. That is to say, when farm land is worth from $100 to $300 an acre or more, it is necessary to practice a type of farming in which there will be a sufficient amount and a proper balance of crop and live stock enterprises, so that there may be the most profitable employment of labor and equipment throughout the year. The income from the farm will in this way be made continuous throughout the year and will be at a maximum, and the fertility of the soil will be maintained.

Many owners, however, require that the tenant confine himself to crop pro-

[2] *Ibid.*, p. 533.

[3] *Department of Commerce Census Monograph*, No. 4, p. 15.

[4] *Ibid.*, p. 13.

duction, and in the South the further limitation of growing nothing but cotton is frequently imposed. The one-crop system is being perpetuated partly because of the inertia of custom and partly because of the mutual distrust with which tenants and their landlords so frequently regard each other. The landlord wishes to insure himself against the pilfering of which he suspects tenants as a class to be guilty; the tenant, on his part, often prefers to raise nothing but cotton, as he is then free to move without serious incumbrance when he becomes tired of the place he happens to occupy, and also he may enjoy a vacation about six months in the year. Many tenants, however, are forced to the one-crop system against their will because of crop liens held by merchants, bankers, and landlords for advances of provisions or credit while growing the crop.

Maintaining the Productivity and Value of the Farm

The central aim of a leasing system should be to maintain a high productivity upon the farm. This is especially desirable from the landlord's standpoint, for with any investment it is more important to keep the principal intact than to obtain an immediate higher rate of return. In the long run, if the productivity is not maintained, the value of the land itself, which is dependent upon the income, must necessarily decline. The failure to recognize this basic principle is strikingly exemplified in the case of the black-land area of Texas. About 20 counties are included in this district, and the soil is unusually fertile. Yet in Ellis County which lies in the very heart of this section and in which most of the land is capable of being cultivated, there has been a gradual downward trend in the yield of lint cotton per acre since 1900, due to soil depletion, boll-weevil infestation, and toxic condition of the soil resulting from continuous growing of cotton.

A statement released from the Texas Experiment Station under date of February 14, 1925,[5] throws a good deal of light upon the present status of farm organization in this area. The statement is as follows:

"Records just completed of the 1924 crops on the Texas Agricultural Experiment Station, at Temple, show that cotton grown in rotation for the past 13 years produced this year more than twice as much as cotton grown continuously on the same land. When summarized, the yields for the past 11 years show that where cotton is grown on land in rotation with other crops, an annual increase in yield of 74% is obtained over cotton which is grown continuously on the land. In the first years of this experiment, the gain made by cotton grown in rotation with other crops was from 40% to 50% greater than the yields made by cotton grown on the same land continuously. But as the experiment progressed, the benefits from rotating cotton with other crops were more and more evident, amounting to as much as 132% in one of the latter years."

Dr. B. Youngblood, director of the Texas Experiment Station system, in commenting on these results, said:

"This remarkable showing for rotation is convincing evidence that cotton should not be grown on the same land year after year and that the best yields of cotton are secured on the black lands by rotating cotton with other crops.

"The black-land area is the chief cotton-producing area in this state. The black lands grow 43% of the cotton acreage of Texas and produce 43% of

[5] Press Bulletin Release No. 178.

the Texas crop. It is realized, since cotton is the chief crop in the black lands, that rotation of cotton with other crops is more or less difficult for the black-land farmer to practice. At the same time, any black-land farmer can so arrange his crops on his farm that his feed crops, and crops other than cotton, will shift on to cotton land each year. For example, supposing a farmer grows 80 acres of cotton and 20 acres of corn and feed, the cropping plan can be so arranged that every fifth year the land will be planted to corn and feed. While this systematic shifting of the feed crop each year will not allow as great benefits in the way of increased yields as those obtained on the Temple-Belton Station, it seems that, in the light of the gains made from rotation, such a plan would result in marked gains in the production of cotton."

The recommendations made by Dr. Youngblood in the above quotation relative to the growing of feed crops in rotation with cotton every fifth year seem extremely conservative, yet, if adopted, they probably would represent a marked advance over present practices.

This land is priced at from $150 to $200 an acre and more in some cases. In areas west and south of the black-land belt, the yields of cotton are almost as great, but the price of land is only one-third to one-fifth as much. In view of the fact that the price of land must ultimately be sustained largely by its economic productivity, it seems clear that something must be done in the near future to bring out the latent powers of this land more effectively than can be done under the present practice of growing cotton almost exclusively.

At present there are in Texas 42 counties in which the percentage of tenant-operated farms ranges from 60% to 73% of the total. The black-land belt and the land adjacent to it include the majority of these 42 counties. That there is need for greater diversification from the standpoint of increasing the productivity of the land is seen in the way the soil responded to diversified cropping at the Temple Station, as described above. The addition of appropriate live stock enterprises in conjunction with a proper cropping system would doubtless still further increase the returns. But the desire for immediate returns to meet the high cost of living restrains the landlord from developing the proper kind of farm organization. The increasing overhead expense and the mounting tax burden conspire to the same end.

Far-seeing landlords, however, are beginning to see the "handwriting on the wall." They recognize that on the basis of present capitalization their land is bringing them a very low rate of return, and that they cannot hope to have this income supplemented indefinitely through a rise in land value—a condition which has gone far to reconcile the owner of black land with his rental income in the past. Should a further recession in the price of cotton occur, which seems likely, there must come either a marked reduction in the price of this land or a greatly improved system of farm organization.

The black-land area of Texas offers a striking illustration of a system of leasing which was adopted when the transition was made from the extensive live stock industry to the more intensive cotton production. In the early eighties this represented a big step forward. The size of farms was reduced and the productivity of the land greatly increased. In the north the first transition was from grazing to grain production, and in recent years gradual progress has been made in the direction of

real husbandry, which embraces crops and live stock in more nearly the right proportions. In both the black lands of Texas and in the fertile areas of northwestern Iowa and the adjacent territory, where the percentage of tenancy is extremely high, the landlords are confronted with the alternative of either developing a more scientific leasing system, or of suffering a serious loss due to the decline in the value of their land.

The University of Illinois recently held its Third Annual Conference of Landowners and Managers. It is worthy of note that this group, many of whom were dealing with 40 or 50 tenants, gave little attention in the conference to the economic relations of tenants and landlords. However, the whole question of more profitable systems of farming, including the place of live stock and the question of soil fertility, attracted much attention. Professor H. C. M. Case, of the University of Illinois, regards this as highly significant. He considers that it is only logical that landowners on the best land in Illinois have given little attention in the past to the organization of the farms, because the natural fertility of the soil was such that practically maximum yields could be secured with little attention to the maintenance of the soil.

However, the turning point has been reached in this respect. There is now definite need of improving the productivity of the land through liming, use of fertilizers, or the keeping of live stock. While it is true that dissatisfactions in tenant farming arise from an unfair division of the returns between the two parties, or to a system of farming that does not permit maximum returns, it is evident that these men consider the latter question to be the more important. The main question in the minds of many of the managers of the larger estates in Illinois is how they may develop a system of farming with the tenant which will maintain or improve the fertility of the land and add to the income from the farm. It is significant that in this group of men were included representatives of several of the largest estates in Illinois. This problem of the landowners, stated above, is prominent in the minds of those responsible for the operation of many of the large estates in Illinois, including the Scully, Sibley, Warner, Fairbanks, and other estates of like size.

A Fair Rent

Maintaining the productivity of the land is, after all, not merely a private affair between landlord and tenant; it is a problem that has public aspects as well. The supply of *good* agricultural land is almost exhausted; more and more we are drawing upon marginal land for the new farms. If an increasing population is to be fed and clothed, the acres now in cultivation must be made more productive, not less fruitful. In other words, it is of deep public interest that landlord-tenant relationships should be such that the fertility of the land is maintained. Society cannot well afford to tolerate a breakdown of the present system of tenure on this point.

However, the experience of the world shows that good agriculture is possible with most of the land in the hands of tenants. The first step in this direction is to inculcate in the public, landlords, and tenants a realization of the situation and a desire to fulfil their mutual obligations. The second step is to develop a leasing system which will be fair to both parties to the contract and which will also bring about good agricultural practice. A fair lease has been de-

scribed as one in which each party contributes to the expenses in the same proportion that he shares in the proceeds. This rule may be applied to any particular farm by listing the items furnished by each party and setting down a cash estimate as to the value of each item.

The old method of entering into a contract on the basis of the "going" or customary rent is almost certain to be unfair to one party or the other. No two farms are exactly alike, and perhaps no two tenants would secure the same results in operating the same farm. Each farm lease should be considered as an entity in itself, and due consideration should be given to the individuality of the tenant and the landlord as well as to the peculiarities of the particular farm. Landlord and tenant relations will be most satisfactory, and tenant farming most profitable, when a proper adjustment is secured with reference to the three important elements in the leasing arrangement, namely, the tenant, the landlord, and the farm.

The lease should be adjusted to the age, farming experience, capital, and business ability of the tenant. This implies that with the passage of time new adjustments in the terms of the lease must be made with the same tenant as he becomes more mature, and acquires more capital, experience, and managerial ability. The competent landlord is the one who will bring out the best that is in the tenant. As a matter of fact, he is the one who, in the first instance, exercises care and prudence in the selection of his tenant, and year by year makes such adjustments in the rental arrangements and the farm organization as to draw out the latent powers of his tenant; and he will, in due time, advise him in the selection and purchase of a farm of his own. Mutual trust between landlord and tenant and respect for each other's rights are essential prerequisites in any successful leasing arrangement. Only in this way can a long-time program in farm organization be carried out, and a fair rent be realized. Wherever this relationship prevails, there is seldom any serious question about the fairness of the rent.

There are forces, however, such as the rapid industrialization of the South and West, which are making for instability of tenancy. Again, the very concept of an "agricultural ladder" implies easy access from one "rung" to the next, and this frequently involves shifting, since advancement often means moving from a smaller to a larger farm. To the extent, therefore, that shifting of tenants and insecurity of tenure complicate the leasing problem, there is little occasion for optimism that these difficulties will soon be removed.

Obstacles in the Way of a Better Leasing System

England is frequently cited as a model which should be followed in working out a better leasing system for this country. But the possibilities along this line are distinctly limited, for the conditions in the two countries are radically different. Both physical and psychic factors contribute to bring about the differences. On the one hand, England is noted for the stability of her tenants and the security of their tenure; on the other hand, a shifting tenancy and an insecure tenure are the characteristics of our tenancy system. In England, a tenant family frequently remains on an estate for many generations. In the United States, it is estimated that 27% of the tenant farms and 6% of the farms operated by owners changed occupants

in 1922.[6] One of the primary causes of shifting in the past has been the presence of an abundance of cheap, virgin land farther west. The importance of this factor, however, will be relatively small in the future. Another factor making for insecurity of tenure is the facility with which landed property may be bought and sold. But opportunities for speculative gains will probably become less and less as the prospective increases in income from land become more and more universally discounted in advance.

The Function of the Landlord

It should be pointed out, in conclusion, that the responsibility for putting into practice a leasing system which will promote conservation of the soil through better farm organization, rests upon the landlord. He holds title to a resource upon which the public is vitally dependent. It happens, through the normal action of economic laws, that the welfare of society is more vitally concerned with the agricultural land upon which the bulk of the leasing arrangements exist than upon an equal area of other agricultural land, because the lands which are characterized by a high percentage of tenancy are generally the most productive. The landlord must justify his right to this important trust.

On account of the pioneer traditions respecting landed property and the exploitation of the soil, landlords, in the main, have not been conscious of their responsibility. The landlord has an important function to perform. He should find the proper person to operate his farm and, having found him, should create a condition that will make it mutually desirable to continue the joint enterprise over a number of years. This is not an easy matter. The unwillingness of landlords to pay the necessary price of finding a suitable tenant and of working out a satisfactory agreement has been mainly instrumental in bringing about the present almost universal inefficiency in our leasing arrangements. In the solution of this problem the landlord has a right to expect assistance from the agricultural colleges. One of the important functions of these colleges is to train men who are capable of undertaking active management of landed estates. Many well-qualified men are now available, and others would prepare themselves for the work if the opportunities promised to be as good as alternative opportunities in other fields.

The improvement of these opportunities waits upon a recognition of the need for applying economic principles to landlord-tenant relationships. In the words of H. Stanley Jevons:[7] "The first step in a satisfactory leasing arrangement is an efficient tenant and a landlord of vision. Landlords must learn improved agricultural methods and then arrange for their tenants to learn them. It is also the duty of the landlords to dismiss bad cultivators, giving compensation for any unexhausted improvements made by them, and to select and encourage those who are the best husbandmen."

---

[6] *1923 Yearbook*, United States Department of Agriculture, p. 589.

[7] *The Economics of Tenancy Law and Estate Management;* Bulletin Number 17, University of Allahabad, India, 1921, p. 25.

THE PUBLIC CONTROL OF HOUSE RENTS

By MARCUS WHITMAN

IN common with many other countries, the United States experienced a housing shortage of such magnitude that it upset the normal policies and practices of dealing with similar situations. Our normal attitude toward the minor dislocations of economic activity that continually recur has been to give free play to private enterprise in reestablishing the balance. But, as in so many countries during and following the war, the major dislocation in the housing industry called forth varying degrees of public interference with private enterprise. Inevitably this departure from normal policy has brought consequences, economic, legal and social, that may or may not prove desirable. Hence, an examination of American experience may be helpful in determining what our future attitude toward housing problems should be. Specifically, a study of the theory and practices of rent control throws light upon the process of transforming a private enterprise into a public utility and upon the best methods of shaping this process to public advantage.

The general economic situation out of which the housing shortage came had a great deal to do with the subsequent course of events. It is not without significance that the housing shortage was the product of war conditions. America's entrance into the war changed radically not only the channels of productive effort, but also the popular attitude toward public control of private enterprise. In the first instance, labor and materials were diverted from the less essential peace-time activities to "war industries." This did not mean a complete cessation of building, but the building was of a different character, suitable for war needs. Among other types of building, residential construction suffered. In addition, the concentration of labor in centers of war industries created an unprecedented demand for housing space. The net results of these readjustments were an acute housing shortage in certain localities and a rapid rise in rents. It is not surprising, therefore, that these conditions of scarcity produced some strained relations between landlords and tenants.

The need of remedying this situation became immediately apparent. What was the best means of protecting necessitous tenants? On every side, in this country as in others, public authority was invoked to alleviate the bad effects of the temporary breakdown of private enterprise. So it was in the housing situation.

The problems raised in seeking to decide just what degree of public authority should be exercised were of three general types—legal, economic, and social.

From the legal point of view, is housing a field of enterprise affected with sufficient public interest to justify temporary or permanent regulation of rentals and rates of return upon the investment? In other words, is housing a public utility? Growing out of this question is the problem of determining the fair value of the property investment on which rates of return are to be fixed. This whole question of what is a fair rent has economic as well as legal significance. If rents are controlled by

public authority, will there be sufficient inducement to new building? Obviously, the only permanent relief of a housing shortage comes from the new capital attracted to real estate investments by the prospect of favorable returns. A lowering of these returns by public control may discourage new capital and delay the reestablishment of a normal balance between supply and demand. From the standpoint of society, rent control may imply either a permanent or a temporary breakdown of competitive enterprise. As urbanization increases, will it be necessary to adopt a permanent policy of public control or public subsidy of housing? Here we find the broad question of the proper spheres of private and public initiative —a question which embraces all other problems and goes to the roots of our economic system as it is illustrated in the housing industry.

I. Types of Rent Control

Rent regulation may be classified according to the source of authority, as national, state, or municipal, and according to the form of administration, whether by statute or administrative commission.

Congress took action in three instances. The Soldiers' and Sailors' Civil Relief Act of 1918 was practically a war measure and merely prevented evictions or distress in the case of premises occupied at a rent of not more than $50 a month by the dependents of soldiers, except where permission had been granted by a court in an action at law.[1] The Saulsbury Resolution of May 31, 1918, was also a federal measure. It was repealed by the Ball Rent Law, which applied to the District of Columbia and was the last of the three federal rent-control measures which were actually passed and enforced with some effectiveness.

The activity of states in rent control has far exceeded that of the Federal Government. It may be classified as (1) specific war-control measures, and (2) general legislation passed to take care of the later war period and the post-war situation. Specific war legislation was confined to but a few states, namely, Maine, Connecticut, Massachusetts, New Jersey, Nevada, and Virginia.[2] The Maine law of 1917 protected tenants in the service from actions at law until after discharge from the service. The Connecticut emergency legislation of 1917 provided for the establishment of Commissions of three representative citizens each, in Bridgeport, Derby, Groton, Hartford, New Haven, New London, Seymour, and Waterbury. These commissions were to aid in settling rent disputes. The Massachusetts act of 1917 was similar to that of Maine. It gave the Governor power through the executive manager of the Public Safety Commission to requisition buildings under certain conditions for public use. The possession of this power by the government proved helpful in inducing landlords to abate unreasonable demands. In New Jersey and also in Connecticut, courts having jurisdiction over eviction cases were requested to suspend judgment whenever the public safety and welfare was threatened as a result of exorbitant demands on the part of landlords. Nevada modified its law relating to notice in month-to-month tenancies, 15 days' notice being required. The Virginia Law of 1918 postponed final judgments in legal proceedings during the period of

[1] Schaub, E. I., "The Regulation of Rentals during the War Period," in *Journal of Political Economy*, January, 1920, pp. 19, 24.

[2] Schaub, *op. cit.*, pp. 12-16.

military service, when one of the parties was in the service.

On the whole, the war legislation concerning rentals and housing was reasonable. It was more conservative than that of France, which not only forbade legal proceedings involving men with the colors, but also provided, in certain cases, for exemption from the payment of rent and for the cancelation or extension of leases. Great Britain and New Zealand were also more radical, for their legislation greatly restricted rental increases and evictions. Legislation in New South Wales also went further than that in this country during the war; fair rent courts were established and definitely instructed with reference to the net returns which might be allowed to landlords.

The most important and effective state rent-control activity came shortly after the end of the war. At this time the cumulative effect of war-time derangements of building activity was at its height, and the housing situation was particularly serious. Post-war rent control was of great importance in New England and in the Atlantic Coast states, because of the prominence of large cities in which the housing shortage was most marked. Chief among the states enacting emergency measures were New York, New Jersey, Massachusetts, Maine, Delaware, Illinois, Colorado, and Wisconsin.[3]

Municipal activity was also an important part of the rent-control movement and was considerably more wide-spread than state activity. The type of control represented by municipal action was not regulation laid down by statute or ordinance; it was based on the strength of public opinion and upon a willingness to cooperate among the citizens. Municipal committees and associations of various descriptions were formed to probe the matter of alleged rent profiteering, and numerous schemes were worked out for the settlement of rent disputes. Among the cities in which local rent control assumed some importance were Fresno, Los Angeles, New London, Jersey City, Atlanta, Chicago, Wichita, Baltimore, Newark, Buffalo, Cleveland, Dayton, Akron, Hamilton, Philadelphia, and Seattle.

The scheme adopted by the city of New London, Connecticut, was unique and fairly successful. A committee of 24 members representing employers, workers, lawyers, and real estate dealers was formed. This committee was divided into groups, called adjustment boards, which heard complaints, determined fair rents, and asked the landlord to appear and show cause for his action when complainant's contention appeared just. If any landlord refused to appear before this board, this fact was published. The success of the New London scheme led to the promotion of similar committees by the division of the Federal Bureau of Industrial Housing and Transportation which had sponsored the New London plan.[4]

Administration of Rent Control

Passing from the classification of rent-control activity based upon the source of authority to that based upon the form of administration, two principal types of rent control may be mentioned. These types stand out most clearly in the control activities of the states.

---

[3] Rasmussen, H., *Regulation of Excessive Rental Charges in the States and Cities of the United States*, Wisconsin Legislative Reference Library, Madison, 1920, p. 1.

[4] Rasmussen, *op. cit.*, pp. 2-7.

Under the first method, control was sought through the legislative modification of the law of landlord and tenant, and these modifications served to guide the courts in settling landlord-tenant disputes as they arose. The statutes of Massachusetts and New York are perhaps the best examples of rent control by a modification of the law of landlord and tenant. The rent-control laws of the various states enacting them are too voluminous and detailed for presentation here. A condensed summary of the New York legislation, although it is considered more far-reaching than that of other states, will serve for illustrative purposes. In brief, the New York laws:

1. Protected tenants against undue increases in rent and empowered the courts to determine the fair rent, and to enforce it;
2. Prevented the dispossession of tenants while a disputed rent was being determined by the courts;
3. Provided for a stay in summary dispossession proceedings at the discretion of the court and allowed tenants to continue their occupancy in view of the housing shortage;
4. Placed upon the landlord the burden of proving a just and reasonable rent in cases of increase, the tenants being allowed to defend themselves in a court action by pleading that the rent asked was unjust and oppressive. [5]

The other major form of rent regulation was carried out through the creation of rent-adjustment commissions. New York, New Jersey, Illinois, Massachusetts, Colorado, Delaware, Maine, Wisconsin, and the District of Columbia at one time or another made use of this latter method of coping with rental problems. Under legislation of the second type, many of the larger cities in the respective states erected their own rent-adjustment commissions. Among such cities were Portland, Oregon, Boston, Seattle, Milwaukee, Denver, Akron, and Dayton. These adjustment commissions were all similar in organization, power, and duties.[6]

The Ball Rent Law of 1919 and the Wisconsin law of 1920 both established the commission type of rent control.[7] The Ball law provided for the appointment by the President of a commission of three men, who were given power to regulate rentals and service in dwellings, business property, and hotels. The commission was empowered to hold hearings, admit evidence bearing on the landlord-tenant disputes, and determine fair and reasonable rentals. Its determinations were to be final unless within 10 days one of the parties to the complaint had appealed from its findings to the Court of Appeals of the District of Columbia. The law also provided that no tenant should be evicted so long as he paid rent fixed by the commission, unless the owner himself or a *bona-fide* purchaser from the owner wished to occupy the premises. The application of this measure was restricted to the District of Columbia, and its enactment was prompted by the necessity of affording some protection to the great number of public employees whose duties required them to reside within the District. The Ball Rent Law, however, was intended only as an emergency measure to soften the effects of a supposedly temporary but serious housing shortage, and ceased to be effective on May 25, 1925.

A bill for a permanent rent commission in the District of Columbia was favorably reported out of committee during the last session of Congress, but

[5] See *Laws of New York*, 143d Session, 1920, Vol. III, pp. 2477, 2478, 2480, 2483, 2485, 2488.

[6] "Rent-Control Legislation in the United States," *National Municipal Review*, 1923, Vol. XII, p. 559.

[7] *Statutes at Large*, Washington, 1919, p. 298; *Laws of Wisconsin*, 1920, C. 16.

was lost in the "legislative jam" at the close of the session. It is interesting to note, however, that the Washington, D. C., Real Estate Board has voluntarily established a committee to consider reported abuses on the part of landlords. Here is an attempt at voluntary arbitration by the private industry most concerned; the progress of the attempt will be watched with interest.

The Wisconsin act of 1920 was similar in general principle to the Ball act. It was limited in its application, however, to cities or counties having a population of 250,000 or more. This stipulation rendered the act applicable to Milwaukee County alone, and was the principal reason for later declaring the law unconstitutional.

II. The Legal Aspects of Rent Control

Rent control in this country formed a substantial addition, for the time being, to the movement for public regulation of certain aspects of economic life, a movement which has been constantly growing since the latter part of the nineteenth century. It was inevitable, therefore, that the legality of rent control would be challenged, and this was done in the cases of the New York and District of Columbia laws. The housing situation in New York City and Washington, D. C., was perhaps more acute than elsewhere, and the rent-control laws applying in these places were undoubtedly as far-reaching as any of the new legislation enacted in this country. The chief constitutional objections against these laws were as follows:[8]

1. That the rent laws deprived the landlord of his property without due process of law in violation of the Fifth and Fourteenth Amendments to the Federal Constitution, because they allowed a tenant to retain occupancy after the expiration of his term or after having been given notice to quit, and denied the owner's right to the possession of the premises except in certain cases.

2. That the laws permitted tenants to remain in spite of their contracts to surrender possession at the end of their terms, and this feature impaired the obligations of preexisting contracts in violation of Article I, Section 10 of the Federal Constitution.

3. That undue discrimination was exercised in classifying cities and buildings for regulation in New York.

4. That the New York law, making it a misdemeanor wilfully to withhold apartment services such as water, heat, and light, imposed involuntary servitude upon the owners in violation of the Thirteenth Amendment.

These objections were all overruled by the United States Supreme Court in a number of leading cases.[9] In these cases the court had to face the problem of defining the limits of the police power. By the weight of previous cases, it was established law that a public exigency will justify the legislature in restricting property rights in land to a certain extent without compensation.[10] The question before the court was whether or not the rent laws under review went too far in this direction. The court answered the question in the negative. The opinion was that in view of

[8] *Block* v. *Hirsh*, 256 U. S. 135 (1921); *Marcus Brown Holding Co., Inc.*, v. *Feldman et al*, 256 U. S. 170 (1921).

[9] *Block* v. *Hirsh*, 256 U. S. 135 (1921); *Marcus Brown Co.* v. *Feldman*, 256 U. S. 170 (1921); *Levy Leasing Co.* v. *Siegel*, 258 U. S. 242 (1922).

[10] *Welch* v. *Swasey*, 214 U. S. 91 (1909); *Plymouth Coal Co.* v. *Pennsylvania*, 232 U. S. 531 (1914); *St. Louis Poster Advertising Co.* v. *St. Louis*, 249 U. S. 269 (1919); *Perley* v. *North Carolina*, 249 U. S. 510 (1919).

the existing circumstances and of the serious housing shortage in New York and Washington, the business of renting buildings was clothed with a public interest so great as to justify regulation under the police power while the exigency existed. In other words, these decisions put housing in New York and Washington on a public utility basis *for the time being.* Housing was thus placed, to use the third classification laid down by Chief Justice Taft in *Wolff Packing Co.* v. *Kansas Industrial Court,*[11] among the businesses which, though not public at their inception, may be fairly said to have risen to be such and have become subject in consequence to some governmental regulation. They have come to hold such a peculiar relation to the public that this is superimposed upon them. In the language of the cases, "the owner, by devoting his business to the public use, in effect grants the public an interest in that use and subjects himself to public regulation to the extent of that interest, although the property continues to belong to its private owner and to be entitled to protection accordingly."

Having established rent regulation as a proper exercise of the police power in controlling a business temporarily affected with a public interest, the remaining constitutional objections were easily disposed of. In *Marcus Brown Co.* v. *Feldman* it was decided that the laws under review did not impair the obligation of contracts, for contracts are made subject to the exercise of the police power when such exercise of the police power has been held proper as was the case here. The objection that the New York laws were discriminatory was also overthrown because the want of shelter was very pressing and so confined to certain crowded centers that the classification was obviously justified. However, the Wisconsin Supreme Court took the opposite point of view when it declared the Wisconsin law invalid. Chief Justice Siebecker felt that the classification limiting rent control to Milwaukee County was unreasonable "in that it is not based on characteristics legitimately distinguishing the members of one class from those of others in respects germane to the public purpose and object of this legislation." [12]

The objection, that the New York law violated the Thirteenth Amendment because it required active services to be rendered to the tenants, was also overruled. The court held that the services in question constituted the universal and necessary accompaniments of modern apartment-house living, and thus they were analogous to, and just as much included in, the lease as were the services that in the old law of property might issue out of, or be attached to, the land.

Is Housing a Public Utility?

It must not be presumed, however, that the Supreme Court upheld rent control as a permanent exercise of the police power. To use the words of Justice Holmes in the Block case, "the regulation is put and justified only as a temporary measure. A limit in time to tide over a passing trouble well may justify a law that could not be upheld as a permanent change." Throughout the cases the court distinctly emphasized the fact that the emergency character of the legislation was its main support. This fact should be recalled apropos of

[11] 262 U. S. 522 (1923).

[12] *State Ex Rel. Milwaukee Sales and Investment Co.* v. *Railroad Commission,* 183 N. W. 687, at 690 (1921).

the recent movement in Washington to place rent control on a more permanent basis, relying not on the emergency argument, but rather on the claim that housing has become permanently affected with a public interest. This raises the question of whether or not the doctrine of the business affected with a public interest may not be carried too far. In that connection the words of Justice McKenna in the Block case are significant. He opposed sustaining rent-control legislation even on the emergency principle. "If one contract can be disregarded in the public interest," he argued, "every contract can be. . . . Does not the decision just delivered cause a dread of such result and take away assurance of security and value from contracts and their evidences? . . . Under the decision just announced, if one provision of the Constitution may be subordinated to that power [police power], may not other provisions be? At any rate, the case commits the country to controversies, and their decision, whether for the supremacy of the Constitution or the supremacy of the power of the states, will depend upon the uncertainty of judicial judgment."

How the Federal Supreme Court will react in case it has to pass upon legislation permanently establishing rent control remains to be seen. The attitude of Justice Holmes in *Chastleton Corp.* v. *Sinclair* [13] seems to indicate a continued belief that such legislation can be supported only as an emergency measure. His words on this matter, though *dicta* in the case, illustrate a definite point of view. "But even as to them" [the lawmakers], he says, "a court is not at liberty to shut its eyes to an obvious mistake, when the validity of the law depends upon the truth of what is declared. . . . A law depending upon the existence of an emergency or other certain state of facts to uphold it may cease to operate if the emergency ceases or the facts change."

The same general attitude of the Supreme Court toward rent control may also be gathered from the opinion of Justice Holmes in *Pennsylvania Coal Company* v. *Mahon*.[14] In this case he restated the old principle that if regulation goes too far, it will be recognized as a taking of property for which compensation must be paid. "A strong public desire to improve the public condition is not enough to warrant achieving the desire by a shorter cut than the constitutional way of paying for the change." The whole question is one of degree, the degree of authority to be exercised and of coercion to be corrected, and, consequently, cannot be settled by general propositions. And Justice Holmes probably sensed public opinion correctly when he said that the New York and District of Columbia laws went to the limit of the law as at present construed.

III. What Is a Fair Rent?

Closely connected with the legality of rent control is the twofold economic question of what is a fair rent and how it is to be determined. A satisfactory answer in all cases proved to be one of the most difficult problems involved in the administration of rent-control laws, and the question is not yet thoroughly solved. Obviously, the determination of fair rents under the emergency legislation was somewhat analogous to the problem of rate-making for utilities under public control, a problem which has been considered in many aspects by the

[13] 44 Sup. Ct. 405, at 406 (1924).

[14] 260 U. S. 393, at 415, 416 (1922).

courts during the last 30 years or more. The fair-rent problem presents many of the controversial complexities of the rate-making problem; so perfection is hardly to be expected in the short time that courts and commissions have been dealing with the problem.

Before considering the practices of courts and commissions in determining fair rents, it will be helpful to discuss briefly the economic nature of housing under both normal and emergency conditions. Ordinarily the renting of homes differs very markedly from providing transportation or warehouse facilities open to public use. In normal situations there is no element of monopoly; there is no substantial evidence of a general concerted movement among prospective builders or among landlords to restrict building and boost rents. Private owners have not combined, and their holdings are too scattered, as a rule, to make monopoly possible in any form. The business of providing houses is not naturally monopolistic, as is, for example, the street-railway business. It has long been recognized that regulated monopoly is the proper form of economic organization for public utilities. This is the theory behind the indeterminate permit and the certificate of convenience and necessity. It is based on the fact that competition among the businesses commonly called public utilities is economically and socially wasteful. Competition among street-railways, for instance, makes duplication of facilities necessary, but it is quite apparent that the dangers of plant duplication do not exist in the housing field.

From a legal point of view, it seems to have been demonstrated that formal rent regulation is primarily justifiable only when emergency conditions prevail. Most of the court decisions emphasized the acute shortage of housing facilities resulting from the shifting of population to the industrial centers and the cessation of building activity during the war. Moreover, the courts recognized that providing homes involved the health, safety, and happiness of so many people as to be, for the time being, highly affected with a public interest. As has been explained, this did not mean that the business of renting houses is generally monopolistic. It simply meant that at particular times and in certain places the demand for housing facilities increased so abnormally as to make it impossible for natural economic forces to increase the supply fast enough to balance the demand. In these instances normal competition is not effective enough to prevent the lag in supply which follows an abnormal demand, and a situation which resembles monopoly prevails. This temporary situation is not the result of the volition of men or the nature of the business, but is the outcome of extraordinary circumstances. Under the circumstances, housing becomes a business affected with a public interest, for "when the coercion residing in private property makes itself felt as a monopolistic power, public interest arises in proportion as equality of opportunity to choose is restricted." [15]

Rent regulation finds its proper sphere, therefore, in a situation that may perhaps be best described as a temporary scarcity or quasi-monopoly. Hence, rent control should not be construed as a means of arbitrarily cutting down rents at the whim of those in power. It is to be used to bring equal justice to all in so far as this may be possible. Control should aim chiefly at eliminating the worst effects of the lag in the supply of dwellings behind the

[15] Glaeser, M. G., "The Meaning of Public Utility," THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS, April, 1925, p. 186.

demand for them. From the economic point of view all that rent control accomplishes is to check "sky-rocketing" of rents which enables some unscrupulous landlords to pocket an extra return simply by taking advantage of the peculiar relation of supply and demand in the emergency.

Under normal conditions a fair return is a price high enough to induce the landlord to continue operating his investment unimpaired and, at the same time, to attract enough new capital to keep the supply of housing facilities balanced with the demand. This is tantamount to saying that a fair return is a normal competitive return for that type of investment. But under conditions of abnormal scarcity, scarcity tends to force the economic return to an impossibly high level for those with stationary incomes. Hence, if the period of scarcity is prolonged and economic coercion is to be prevented, the fair return must be fixed between the normal competitive return and the high scarcity return which would result from the free play of economic forces. Just what point below the scarcity return marks the level of fairness is a matter both of relative justice—a moral judgment—to landlord and tenant, and of economic judgment. From the moral point of view a fair return will prevent extortionate rents; from an economic point of view a fair return will not discourage the normal flow of new capital into building construction in order to correct the lag of supply behind demand. To determine a practical, usable method of finding this point was the task of courts and commissions in rent cases.

Determining the Base for a Fair Return

In determining the fair rent of particular premises, the first problem is, in the technical language of public utility valuation, the selection of a proper rate base. In the actual cases which have arisen, the value of the land has not been determined separately. A scientific valuation should probably treat land and buildings separately because different factors have to be considered in determining the value of each. Since cost of production and reproduction are not standards applicable to land valuation, it follows that reasonable market value is probably the most practical standard. By this standard past sales of the same or of contiguous property are considered together with the type of residential use to which the land is being put. If land had been valued separately in the rent cases, the rule would probably have been to take the reasonable market value as determined by the evidence submitted—in other words, a "normal" market value.

The larger and more important problem in arriving at the rate base lies in determining the method of building valuation. Among the chief theories of building valuation are:

1. The cost, or investment, theory;
2. The cost-of-reproduction theory;
3. The market-value, or purchase-price, theory.

There seems to be a diversity of opinion as to which of these valuation standards may best be used. The courts have not seen fit to accept the investment standard unless the buildings in question are comparatively new. In *Karrick* v. *Cantrill*[16] the court held that in view of the newness of the building, cost may be considered equivalent to market value, but that ordinarily such would not be the case. The United States Supreme Court in this case seems to go

[16] 277 Fed. 578, at 580 (1922).

on the theory that a fair rental depends on the market value of the property. Theoretically, cost of reproduction minus depreciation appears to be a fairly equitable standard for housing valuation, though it has been expressly subordinated to market value by the courts.[17] However, it is circular reasoning to make actual or market value alone the basic standard, for that value during the housing shortage was brought about by the very same conditions which the rent laws were designed to counteract. That this fact was apparently recognized by the courts to some extent is shown by their preference for evidence of market values existing before the abnormal period began. Cost of reproduction minus depreciation was objected to on the ground that this value was influenced by the high price of building materials during and after the war. But even so, values based upon the high cost of building materials could hardly exceed values based upon the possibility of obtaining rentals in a market where competition had virtually ceased. The cost-of-reproduction standard assumes that normal competitive conditions and prices prevail. If such conditions do prevail, a value based upon cost of reproduction approximates a competitive price, and is appropriate in the case of buildings, which, even though they are proper subjects of public utility control at times, belong in the field of competitive production.

Some authorities advocate the use of assessed value as a standard. But this method also has its shortcomings, in view of the fact that assessed and actual values are not always the same, even when the added scarcity value brought about by the emergency is deducted from actual value.

In actual practice the courts, though favoring the market-value standard of valuation, did not blindly follow it. They realized that they were being called upon to act in an emergency, and, consequently, they aimed to do justice in each particular case surrounded by its own peculiar circumstances. The general purpose in valuation seems to have been to approximate normal competitive conditions, and this they sought to accomplish through the guidance of a valuation rule similar in some respects to that laid down for public utilities in *Smyth* v. *Ames*.[18] Thus, in ascertaining the fair market value, the courts admitted evidence bearing upon the following factors:[19]

1. Investment
   (*a*) Original cost and additions
   (*b*) Purchase price
2. Cost of reproduction
3. Fee and rental value
4. Assessed value
5. *Bona-fide* sales value of similar property in the vicinity
6. Design and facilities of building
7. Location with respect to purpose for which it was used

To sum up, the general valuation rule of the courts appears to have been the minimum market value of the premises that could be reasoned from the evidence submitted. It can hardly be said that the courts, taken as a whole, have erred seriously in the matter of valuation. They have recognized the emergency character of regulation. Their opinions imply recognition of the fact that the housing shortage can best be relieved

[17] *F. H. Smith Co.* v. *Verzi*, 290 Fed. 338 (1923); *Hall Realty Co.* v. *Moos*, 192 N. Y. S. 530, at 535 (1922).

[18] 169 U. S. 466 (1898).

[19] These criteria of value are gathered from the opinions of courts in several cases: *Karrick* v. *Cantrill*, *op. cit.*; *Forster* v. *Eliot*, 282 Fed. 735; *Hirsch* v. *Weiner*, 190 N. Y. S. 111 (1921); *Hall Realty Co.* v. *Moos*, 192 N. Y. S. 530 (1922).

by private initiative and capital competing in the housing field. Consequently, acceptance by the courts of a valuation which represents fair market value before the inflation resulting from abnormal scarcity had occurred, indicates their aim to insure a competitive return to a normally competitive business where the competitors, through the force of circumstances, have acquired temporarily the price-exacting powers of monopolists.

The Rate of Return on Housing Investments

Determining the rate of return to be allowed upon the "fair value" is the next problem in determining fair rent under the emergency legislation. It seems clear that the rate of return should be high enough to afford the owner the current rate of interest upon the fair value of his building. It should also allow compensation for additional risks taken and entrepreneurial effort expended. The attitude of the courts in general in recent cases seems to be based upon this theory.

In fixing the fair legal rate of return, it was held proper to take notice of the general rate of interest on undoubted securities.[20] The rate in each case was determined with respect to the circumstances which surrounded the particular case. "It would necessarily vary with the market fluctuations of the rates of interest or return on other classes of investment."[21] "The investor in real estate, if building of houses is to be encouraged, should at least get as much income from real property, with all its attendant trouble, as the investor in mortgages on realty and franchises."[22] In *Hirsch* v. *Weiner* it appeared that at the time of the determination (August, 1921) first mortgage coupon bonds were yielding from 8% to 8½% in New York City. Consequently, the court was of the opinion that rent was not unreasonable if it yielded a net return not in excess of 10%. The court carefully pointed out, however, that "such a percentage might be excessive, if the evidence showed a different situation regarding other investments." In two later New York cases where the rate of interest upon undoubted securities was used as a guide, it was held that under the then present circumstances 8% was a fair rate of net return.[23]

In *Karrick* v. *Cantrill,*[24] a Washington case, it was held that in view of business hazards and the value of money at the time (February, 1922), the net rate of return might drop as low as 6% before the line of confiscation was reached. Court authority stops if rates are legally reasonable, that is, above the line of confiscation. But rates which are reasonable at law may not be reasonable from the economic point of view. The economic reasonableness of rates of return involves a question of policy, to be solved by the courts where they have exclusive rate-fixing power, and by commissions or other administrative bodies where courts have merely power of judicial review. This problem was appreciated by the court in *Kennedy Bros.* v. *Sinclair,*[25] a Washington case. "If that was the purpose of the commission [to cut income as close as possible to the line of confiscation] we do

[20] *Olin J. Stephens, Inc.*, v. *Am. Real Estate Co.*, 279 Fed. 435, at 437 (1921).

[21] *Hall Realty Co. v. Moos, op. cit.*, at 537.

[22] *Hirsch* v. *Weiner, op. cit.*, at 116.

[23] *Olin J. Stephens, Inc.*, v. *Am. Real Estate Co., op. cit.*, at 440; *Hall Realty Co.* v. *Moos, op. cit.*, at 537.

[24] *Op. cit.*, at 582.

[25] 287 Fed. 972, at 977 (1923).

not hesitate to say that should the very great power vested in that tribunal continue to be exercised in such a way as to reduce the income from buildings to a point that barely avoids confiscation, investment in that class of property will inevitably cease to be desirable and the second condition of tenants will become more burdensome than the first.

"Price-fixing and rate regulation of purely private enterprises necessarily interfere with the law of supply and demand, and, even when most carefully, prudently, and justly done, generally result in economic complications and social disorders worse than the evil sought to be remedied. That result must always follow if the arbitrament of prices or rates breeds distrust, discourages capital, or diverts it to less beneficial although safer investments."

In practice, the difference between a merely legal and economic rate of return upon dwelling property was often lost sight of by the rent-fixing bodies. It was sometimes forgotten that rent control was not to be so used as to discourage the real solution of the housing problem, which is the entrance of new private capital into the field. The possibility of such a mistake by rent-fixing bodies was not important in New York, where the rent laws applied only to premises then in use for dwelling purposes, and not to buildings of whatsoever character which were under construction on September 27, 1920, or were commenced thereafter. In Washington, however, control applied to new buildings as well as old. It is significant to note in this connection that in the last six years there have been very few houses or low-priced apartments built for rent in Washington. Whether rent regulation was or was not responsible for this situation, it must be remembered that such control, to be justifiable, must not only curb monopolistic exploitation, but must at the same time approximate competitive conditions in its allowance of rates of return and thus avoid discouraging reentrance of private capital into housing enterprises.

Allowable Operating Expenses

After the determination of fair net rental comes the question of what charges may properly be allowed as operating expenses and thus be a part of the gross rentals which tenants have to pay. In general, allowable operating expenses include:[26]

1. Payments for taxes, water rates, insurance, and janitor service;
2. Necessary legal expenses incurred by landlord incidental to maintaining his right to possession;
3. Necessary payments actually made for collecting rents;
4. Payments for necessary supplies incident to the use of the premises, such as coal, gas, and electricity;
5. Payment for necessary current repairs for the year;
6. Allowance for loss of rent by reason of vacancies or tenant failing to pay;
7. Allowance for annual depreciation, if established by proof.

Although the above list lays down the general limits for the allowance of operating expenses, in practice questions have arisen as to whether a particular item of expense in a particular case could be classified under any of the general groupings and to what extent. Thus in *Hall Realty Co.* v. *Moos,*[27] it was held that federal and state income taxes, since they are taxes upon profits as such and not upon land and buildings in the sense of property taxes, were not operating expenses that should be paid by the tenant in rentals. In the same case

[26] *Hirsch* v. *Weiner, op. cit.,* at 116.

[27] *Op. cit.,* at 536.

the court disallowed, as operating expenditures, salaries paid officers of the landlord corporation. It did not appear that the salaries represented payments actually made for collecting rents; so the holding upon this point is not inconsistent with the rule in *Hirsch* v. *Weiner*.

The allowances for current repairs also have complexities. In *Hirsch* v. *Weiner*,[28] it appeared that a new boiler, awnings, window shades, and new plumbing had been installed in the apartment building in question. A new floor on the roof had also been laid, and new electric wiring had been installed. The court held all these items properly allowable as current repairs, although it was contended at the time that the items for boiler, shades, and plumbing were properly distributable against the earnings over a period of years, and that the items for the new floor and the electric wiring should be charged against the depreciation reserve and capital account, respectively. It seems quite clear that repairs which are in their nature recurring are properly allowable. But, on the other hand, it seems equally clear that the financial burden of repairs of a more or less permanent character—replacement and new installations—should not be entirely borne by the individuals who happen to be paying rent during a particular year. One group of tenants can hardly with justice be expected to pay for improvements which will be enjoyed by their successors if they vacate the premises shortly after the improvements have been made. Furthermore, the position of the court seems inconsistent, for while allowing the items for these more permanent replacements as current repair expenses, at the same time it permitted the building owner to accumulate a depreciation reserve out of current income.

In the matter of allowance for loss of rent by vacancy or failure of tenant to pay, the opinion was that no deductions should be made by a court unless evidence of proof is offered.[29] The same rule as to necessity of proof also applies in the case of deductions for services rendered by agents.

With respect to depreciation, the court, in *Hirsch* v. *Weiner*, allowed an annual charge of 2% upon the value of the building. However, in another case[30] the court recognized that no fixed percentage for depreciation can properly be made applicable in every case. The allowable rate is a matter to be determined in each case and must depend upon proved facts and circumstances.

A number of other matters affecting rental values were considered in the determination of fair rents. In practice the rule of the courts was that premises be considered unencumbered in ascertaining the fair rental value.[31] This practice is not as objectionable as it seems. It is true that the landlord receives the differential between the rate of interest he pays and the rate of return he is allowed. This differential is a profit that he makes from trading on his equity, but nevertheless it is, in large measure, merely compensatory for additional risk-taking and entrepreneurial activity in connection with the borrowed money. The logic of the situation is made clear by an extreme illustration. Assume that a building is constructed entirely with borrowed capital and is mortgaged to the extent of the amount borrowed. If the principle of allowing

[28] *Op. cit.*, at 116.

[29] *Kennedy Bros.* v. *Sinclair*, *op. cit.*, at 973.

[30] *Hall Realty Co.* v. *Moos*, *op. cit.*, at 536.

[31] *Hirsch* v. *Weiner*, *op. cit.*, at 114; *Hall Realty Co.* v. *Moos*, *op. cit.*, at 537.

a net return only upon the owner's equity were followed, the owner would receive no net return whatever in this case. Rent would just cover operating expenses. Such a system might seem desirable to tenants, but it would not induce others to build houses. Furthermore, if all premises were not considered as though unencumbered, tenants of similar properties might find themselves paying very different rents in case one property were unencumbered while another was heavily mortgaged. Also, the practice of considering premises unencumbered makes it unnecessary to allow interest as an operating expense and to determine broker's charges and other costs in connection with procuring loans.

Another question of some importance is that of properly apportioning the total rent charge among the several apartments when rent is being fixed for multi-family dwellings. The courts seem to be uniformly of the opinion that the landlord is entitled to a fair rent from each apartment based upon the proportion which the value of each apartment bears to the entire value of the property, regardless of what rent other tenants may be willing to pay. [32] However, in practice, this rule of apportionment does not clear up a difficult problem based upon the human equation. Even though in a physical sense all apartments on a certain floor are of equal value; nevertheless some are corner apartments, some are in the rear, some are in the front. Tenants being as they are, the desirability of these apartments varies with their location. If these apartments were to be rented, free from control, their differences in desirability would normally register in the rents asked. Under regulation the same principle may properly be recognized even though the total rents of all apartments are restricted to a fair return on the value of the property as a whole.

A problem also arises when the value of the building is out of proportion to the value of the land. Such cases often occur in a section which is in transition from a residential to a business district. Often during this "ripening" period old residences on the land are occupied by tenants. In such cases as these the rate of return allowable on the land may properly be reduced, for it is highly unfair to grant the landlord the same return on his land separate from a building of small value as would be granted the owner of a similar piece of land which was being economically utilized for a million-dollar building.

Nowhere have the courts elaborated a complete, well-rounded theory of fair rent determination. They could hardly be expected to do so in the few years during which such cases frequently came before them. Only by a process of piecemeal construction from various opinions is it possible to approximate what appeared fair and reasonable to the courts. In general, the judicial attitude toward fair rents is very similar to the attitude toward rate-making for other public utilities; the courts strive to bring down scarcity rentals as close as possible to competitive rentals. From a strictly economic point of view this may not have been the best theory, if rent control were intended to stimulate new building. But from an equitable point of view competitive standards were probably the fairest and most reasonable, in view of our economic traditions and institutions. However, this theory should frankly be based on the fact that rent control was a palliative and not a fundamental remedy.

[32] *Karrick* v. *Cantrill, op. cit.,* at 581; *Olin J. Stephens, Inc.,* v. *Am. Real Estate Co., op. cit.,* at 436; *Rust* v. *Tucker,* 287 Fed. 1018.

IV. Rent Control and the Housing Shortage

The social significance of rent control lies in its contribution to the solution of the housing problem. An objective appraisal of this public policy is difficult; not only are important economic interests arrayed against each other and the controversies sharp, but also the data on housing that are pertinent to the question of control are conspicuously lacking. A few general observations, however, may make a better perspective easier.

In the first place, there has been much misunderstanding of the real nature of the housing shortage. According to a report prepared under the direction of Professor Lindsay, of Columbia University, the increase of housing facilities in New York City was more than enough to take care of the increase in population between 1910 and 1920.[33] In Massachusetts also, according to the Special Commission on the Necessaries of Life, there was no actual shortage in the total number of houses physically necessary to shelter the whole population.[34] Nevertheless, a real housing emergency came to exist in these places because of the fact that the supply of particular types of housing was thrown out of balance with respect to the corresponding demand. The increased incomes which were characteristic of the war period precipitated a demand for better housing, whereas there had been a cessation of new construction during the war period. So, although the housing shortage so much talked of was not physical, it was an economic shortage in the sense that the supply of the desired kinds of housing had become inadequate. Furthermore, a shortage developed in the sense that the margin between the number of housing accommodations needed and the number existing dwindled perceptibly. Conditions are not normal for the operation of the law of supply and demand in the housing field until there are more good housing facilities than are actually required. Merely enough apartments to accommodate tenants will not do. The supply offered on the market must be large enough to afford a choice; otherwise, the prospective tenant will find himself unduly restrained. Such was the situation which led to the control movement.

The facts with respect to the general building increase seem to indicate that the shortage of housing facilities is now being made up. Actually the question of whether or not the economic shortage is being overcome can be answered both affirmatively and negatively. The first point to be recognized is that housing as a whole cannot be put in one class when the question of making up the housing shortage is being discussed. Different problems arise in connection with the supplying of the various grades of housing, and different economic phenomena must be taken into consideration. Various types of housing may be built, all depending upon particular local conditions. The three-group classification made by the Massachusetts Special Commission may be used as an illustration.[35] The first group embraces high-priced property, where heat, hot water, and janitor service are furnished to tenants, and the rents are over $80 a month. In the second group is put property consisting mostly of unheated apartments in one, two, or more family houses, rents ranging from about $40 to

[33] Lindsay, S. M., *"Some Economic Aspects of the Recent Emergency Housing Legislation in New York,"* 1924, p. 106.

[34] *Report of the Special Commission on the Necessaries of Life,* Boston, 1925, p. 35.

[35] *Op. cit.,* p. 41.

$80 a month. The third group includes property renting for less than $40 a month. The increase in building activities in Massachusetts, New York, and Washington, D. C., during the period of housing control since 1920 seems to have been confined to the upper grades of housing. In Massachusetts acute shortages of property renting for over $60 a month have been greatly relieved.[36] In New York City and Washington, D. C., the dearth of the same types of housing is being rapidly made up. Tenants who can afford to pay rent that will yield a reasonable return upon the owner's investment find that buildings are forthcoming despite building costs which are practically double what they were before the war. Rent control has apparently neither cut off nor accelerated the supply of these better types of housing. However, it is quite apparent that the emergency legislation did protect the tenant from some of the excessive charges during the period in which even the supply of the upper grades of housing was not normal. At present there is no serious problem connected with the supply of the better housing facilities. Those who seek these types of accommodation must simply realize that at present price levels houses represent a heavy investment and consequently require a high rent.

Shortage of Workingmen's Houses

But there is still a serious problem in connection with the type of housing in the third group of the Massachusetts classification, which can be rented for less than $40 a month. In many localities the kinds of homes which the average American workingman needs are not forthcoming in sufficient quantities. There is still a real economic shortage of housing facilities which are within reach of the wage-earner's income, not only in Massachusetts but in New York, Washington, and elsewhere in the large industrial centers.

The real causes of this shortage, however, are frequently not fully realized. When the facts are examined, it can hardly be said that rent control is responsible for this shortage. The truth of the matter probably is that the rents which working people can afford to pay are not high enough to attract capital to workingmen's houses as long as present building costs prevail. If this is the case, it is clear that rent control would have no influence either way upon the situation. Under control, the owner is at the least allowed a fair return upon his investment, but such an allowance is meaningless when prospective tenants can barely afford to pay enough rent even to meet it, to say nothing of paying higher rents.

The crux of the matter apparently is that working people are demanding better housing standards but have not the incomes to pay for them at present price levels. The Department of Labor studies of wage rates of 894,343 unionists in 66 cities revealed an average hourly rate of $1.03 in May, 1924. With the average number of hours worked per week at 45.9, the average week's earnings were approximately $47. This figure represents the earnings of a fairly high class of worker. The average weekly earnings of factory employees in New York State were estimated at $28.30 in January, 1925, the highest figure since December, 1920. The corresponding weekly earnings in Illinois were $28.13 in February, 1925. In Massachusetts similar figures for December, 1924, covering 453 manu-

[36] *Op. cit.*, Special Commission on Necessaries of Life, p. 38.

facturing establishments, were $28.57. If we assume 52 weeks' work during the year (which eliminates layoffs, unemployment, and vacations) the average annual earnings, based on the above figures, would range from $1,462 to $2,444. How much of these annual incomes is or should be paid for shelter? The National Industrial Conference Board family budget allows 17.7%; other budgets allow a greater percentage. Allowing a reasonably conservative 18%, the average worker, with employment throughout the year, would spend approximately from $22 to $37 a month for rent. With the worker's housing standards as they are, such rentals will hardly pay a normal return on an investment at present price levels.

It is difficult to see how rent restriction can ever remedy a situation that is so fundamentally out of balance. Rent-control legislation in some individual cases may prevent undue hardship, yet in general such legislation is unnecessary, for high rents cannot well be exacted when reasonable rents can hardly be paid. What is needed is a stimulation of new housing at low costs per room, and in the nature of the case the prevention of higher rents by legislation does not of itself furnish the necessary stimulus.

If rent control is no remedy, what is the proper and permanent remedy for the housing shortage? It is outside the scope of this article to discuss this question, but, in order to place rent control in a better perspective, it will not be inappropriate to mention a few suggestions that have been made. These suggestions reveal by contrast the preventive, rather than the remedial, nature of rent control.

The proposals that have been made for relieving the housing shortage fall generally into four classes: (1) Reduction of building costs by eliminating some of the inefficiencies of the construction industries; (2) reduction of material costs by scientific planning of land utilization; (3) change of the trends of urbanization and industrialization; (4) public assistance in the form of housing subsidies or governmental construction of housing.

It has been suggested that overhead costs can be materially lessened by building houses through realty organizations which take care of legal, architectural, and financial burdens in a scientific and economic way.[37] No doubt there may be real economies in uniting under one management the functions of the lawyer, architect, and building financier, each one of whom when working unattached is thinking mainly of his individual profits. Even with more efficient building and financial organizations the problem of high direct construction costs remains. Looking toward the solution of this problem various suggestions have been made for improving the distribution and use of labor power, for the standardization of building materials and practices, and for the use of large-scale production methods of building.[38]

One of the chief obstacles is high building material prices. Can more economical methods of using building materials be devised? Can cheaper but efficient substitutes be developed? Experts are working out solutions along these lines, but from the long-time point of view more fundamental remedies must be sought in scientific policies of land utilization. For example, refores-

[37] "Demand for Small Houses Increasing," *National Real Estate Journal*, January 26, 1925, p. 38.

[38] See Gries, J. M., "Housing in the United States," THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS, January, 1925, p. 28.

tation [39] and taxation policies, city and regional planning, a land inventory and classification, all have a bearing upon the problems in question.

The concentration of population and industry in cities has also contributed to the difficulty of building low-cost homes. At present there is a decentralizing trend in some localities—a movement of population and industry to smaller communities, where the possibility of low-cost housing may be greater.

Finally, we find proposals that public initiative supply the remedy, instead of private initiative. Such proposals sometimes view the housing shortage as one aspect of the general problem of poverty. According to Professor Pigou, [40] when economic conditions are such that despite the best efforts a particular group is unable to secure the necessities of decent living, the welfare of that group becomes the obligation of society as a whole. This means state subsidies of housing or state construction of housing. England has been experimenting with state-assisted housing since 1919. At present state aid is being given under the Chamberlain Act of 1923 and the Wheatley Act of 1924, the latter statute continuing the policy until 1939. Some European communities may be cited as illustrations of public construction of houses. Both these policies are premised upon the breakdown of private enterprise in housing.

This brief mention of suggested remedial policies is not exhaustive nor is it intended to show either approval or disapproval. It merely shows that the problem is a fundamental one in our economic system. Moreover, the true nature of rent control becomes more apparent.

What Rent Control Accomplished

Rent control, with its accompanying emergency legislation, was not introduced to solve the housing problem. It was introduced merely to stave off the bad effects of the breakdown of competition in the housing field which followed the cessation of building activity and the soaring of price levels during the war. It aimed to restrain landlords from taking advantage of a situation of temporary quasi-monopoly in the housing field, resulting chiefly from economic disruptions caused by wartime conditions.

On the whole, rent control accomplished its real purpose. Within reasonable bounds it secured justice for all. It protected tenants from the possibility of unreasonable exploitation. It restrained landlords from taking advantage of a situation for which they were not responsible but by which they could have profited greatly if unrestrained. But while performing this negative function of restriction and protection, rent control did not seriously impede the efforts of the housing industry to get back upon a normal, competitive basis. In fact, as appears in the section on fair rent, it aimed, when properly administered, to simulate competitive conditions, to allow a fair return upon the fair value of property. And, in fact, while and where the emergency legislation was in force, the housing situation actually did improve. The supply of the better types of housing is steadily becoming more normal.

On the other hand, the economic shortage of workingmen's dwellings is not to be laid at the door of public

[39] See Greeley, W. B., "Economic Aspects of Forestry," THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS, April, 1925.

[40] Pigou, A. C., *Essays in Applied Economics*, London, 1923, p. 112.

regulation. The responsibility for this shortage lies in the very nature of our economic system. The whole trouble lies in the economic maladjustment under which the income received by many workingmen is frequently insufficient to allow them to purchase the desired shelter in view of the cost of providing such shelter. This, then, being the real nature of the workingmen's housing problem, it is clear that rent regulation as we know it in this country has no great influence one way or the other. It does not tend on the whole to restrict the supply of facilities, for when in force it allows a reasonable rental, and that is more than many workingmen can pay. On the other hand, being principally negative in operation it does not actively aid in supplying more housing facilities.

After all, then, rent control served its purpose reasonably well. While being used, it was improved and developed into a serviceable protective structure which can and perhaps should be used again if the occasion demands. But now that conditions are approaching normality, men can more profitably turn their attention from the protecting structure of rent control to the actual field of workingmen's housing which at present needs, not protection, but cultivation.

DEPARTMENTS

The departments of the JOURNAL are edited specifically with regard to their interest to the readers who are especially concerned with the economic problems of land and public utilities. For the most part the material for the departments will be prepared by members of the staff of the Institute for Research in Land Economics and Public Utilities.

BOOK REVIEWS

This department contains critical reviews and brief notices of new books of interest to the readers of the JOURNAL.

WILLIAM G. RAYMOND, "The Public and Its Utilities," ..... *M. G. Glaeser* 363

JAMES B. MORMAN, "Farm Credits in the United States and Canada" ..... *B. H. Hibbard* 364

L. B. SCHMIDT and E. D. Ross, "Readings in the Economic History of American Agriculture ..... *Mary L. Shine* 366

EDITH ELMER WOOD, "Housing Progress in Western Europe" ..... *Gertrude Harley* 366

E. C. BRANSON, "Farm Life Abroad" ..... *G. S. Wehrwein* 368

SUMMARIES OF RESEARCH

In this department are given brief accounts of investigations in progress and statements of tentative conclusions reached in the course of work by the staff of the Institute and others associated with the Institute's work.

Multi-Family Housing Units and Urban Tenancy .. *Gertrude Harley* 371

Dividend Record of Gas Utilities ..... *W. G. Maas* 372

COMMENTS ON LEGISLATION AND COURT DECISIONS

Here the readers of the JOURNAL will find a miscellany of summaries, interpretations, and notices of recent legislation and court decisions that have economic significance in land and public utility problems.

Judicial Status of Arbitration of Public Utility Labor Disputes ..... *E. W. Morehouse* 375

The Exemption of Homesteads from Taxation ..... *O. M. Johnson* and *B. W. Allin* 380

BOOK REVIEWS

Raymond, William G. THE PUBLIC AND ITS UTILITIES. *New York: John Wiley and Sons, Incorporated. 1925. pp. xii, 346. $3.50 net.*

THE number of works aiming to give a general introduction to the field of public service enterprise has been increasing in recent years. The above-entitled volume presents the subject-matter under four headings:

"1. What are the principles which should govern in establishing rates for service?

"2. What are the bases for, and the nature of, proper public control and regulation of privately owned public utilities?

"3. What constitutes a fair rate of return?

"4. How is the basis of this return, that is, the fair value of the property used in the service of the public, to be determined?"

In an introductory chapter the author first makes clear the distinction between ordinary private enterprises and those having a public utility character, the distinction being drawn upon legal premises. In two short descriptive chapters the author next presents a picture of the creation of a public utility business, of the character of operations carried on by the more common types of local public utilities, and of the nature of the more common revenue and expense items. It is of interest in this connection to note that he uses the illustration of a publicly owned plant in order to bring home the necessity of certain forms of capital outlay that have been the subject of dispute in connection with private enterprises.

The general subject of depreciation is next covered in a series of chapters, the treatment emphasizing the economic, engineering, and accounting aspects. One may question the wisdom of discussing the related technical subjects that suggest themselves, such as the explanation of the fundamental concepts of accounting. Then follows a brief discussion of sinking and emergency funds, and of taxation of utilities both publicly and privately owned. The remaining two-thirds of the work the author devotes to the heart of his subject: (1) the discussion of rate systems, illustrated particularly in the fields of electricity, water, and gas supply, (2) valuation of public utilities, (3) the fair return upon the valuation.

Between the discussion of rate-systems and the general subject of valuation the author has inserted certain materials that seem to this reviewer to fall outside the logical order of the author's own plan of presentation. We find here a discussion of the financing and organization of public utility companies, of franchises, control of capitalization, control of service. Then once more the author comes back to control of rates by public authority, with special emphasis upon sliding scales. In an appendix the book is equipped with the usual complement of amortization tables and illustrations of operating statistics.

Upon the mooted question of valuation the author appears to incline to the prudent investment theory, although he presents and explains what is the current practice under the rule of *Smyth* v. *Ames*.

Again we must say that although much useful information is presented in

this work, the subject-matter as a whole is not presented in a way to afford the student an organic theory of regulation. It may be that the time for such a treatment has not come, or that the ordinary college text does not provide sufficient scope—along with the other things it must do—for such an undertaking. Yet the need for such a treatment is most urgent.

MARTIN G. GLAESER

Morman, James B. FARM CREDITS IN THE UNITED STATES AND CANADA. *New York: The Macmillan Company, 1924. pp. xv, 399. $3.50.*

THIS is the second volume by the same author in the Rural Science Series edited by Dean L. H. Bailey. No mention is made in the later volume of the earlier one. Presumably it is intended that the later volume replaces the former. Of necessity the two volumes, under similar titles, cover much the same ground. As a compendium of information, the present volume is both accurate and useful. Part I deals with farm-mortgage credit; Part II with short-time and intermediate credit. Mr. Morman has analyzed with care and skill the Federal Farm Loan Act and its workings. The subject of amortization is treated, not merely incidentally, in its relation to the welfare and work of the borrowers; it is given a whole chapter by itself. Likewise, the question of government aid for farm-mortgage credit is made the subject of a chapter.

State systems of credit, some 13 in number, are taken up separately and given sufficient space to cover the salient features. In no other single volume is so much information to be had on the plans and operations of farm credit. The treatment which this book gives to the Canadian situation is similar, in care and clearness, to that given to the federal and state influence and action in this country.

One of the outstanding features of this book is the view of the author respecting the nature of agricultural credit *per se*. To him credit means primarily debt, and debt means burden. The dedication of the book to the farmers of the country "who are out of debt" suggests strongly that the author looks upon that condition as the ideal. No doubt it is an ideal to be reached, if possible, by each individual ultimately. However, if young men are to advance beyond the tenancy stage as farmers, they are going to prefer to purchase under mortgage, rather than await the time when they will be able to pay cash for the whole amount of the value involved.

A large number of farmers may be surprised to read that it is the usual expectation on the part of either creditor or borrower that a mortgage is finally to be paid off at the end of the three- or five-year term for which the majority of mortgages in the past have been written. Mr. Morman says: "During these years a farmer lives in dread of foreclosure as the term of the mortgage draws near." Surely this hardly characterizes the state of mind of the great number of mortgaged American farmers during the past half-century. However, within the period of the present depression, the statement is not so wide of the mark.

Incidentally, Mr. Morman drops in here and there a statement of his economic beliefs and views, with some of which many economists will not altogether agree. For example: "From the agricultural point of view, the actual value of land lies in its fertility .... the landlord reaps his reward without labor." This latter view, of course, has

many supporters, but how about the owner of bank stock reaping reward without labor? Again we read: "Rent is calculated on the basis of the prevailing high prices for farms." This dictum will give pause, a short one, to the economist, and will puzzle beyond recovery the landlord who believes it to be a statement of the truth.

Some doubts may arise from the reasoning bound up in the assertion that a farmer in borrowing for land and capital equipment "assumes a double responsibility due to capital deterioration and the payment of interest." Surely all borrowed capital is subject to deterioration the same as capital bought and paid for out of one's own accumulations, no more, no less. The farmer understands this as well as any one. Mr. Morman says: "In this case the basis of interest does not rest directly on the use of money but on the use of land and operating capital for which the money was expended." Why not say "in this case, as in substantially all others?" But Mr. Morman is not to be misunderstood. He closes the discussion with the words: "By no possibility, therefore, can a farmer with a mortgage escape this double drain on his income," the inference being that were the property in question paid for, the deterioration would not be a drain on income at all.

In discussing the recent increase in farm-mortgage debt, Mr. Morman finds from a certain report that a large part of the money borrowed was for paying off old mortgages and recent personal indebtedness, and a small portion used for buying land and making improvements. He infers that the portion used for paying old mortgages will constitute a drain on income, while only the latter sums, for buying land and making mprovements, can constitute a basis of increased income. But would it not be a good idea to look into the character of the old mortgages? No doubt many of them were given on the occasion of buying land. Mr. Morman's conclusion will not be generally concurred in unless it be assumed that buying land is a productive investment if all obligations are paid off in three to five years.

Under the heading, "Farm debt and community welfare," Mr. Morman states that money borrowed locally may be paid back without community loss, but not so if it comes from outside the community. He says: "While outside credit may seem advantageous at the beginning because of supplying needed funds in time of emergencies, in the end it will inevitably impoverish any rural community whose needs have to be financed in this manner." If the community should happen to be sub-marginal, what it had to start on would no doubt grow less through the payment of interest. Should it be a community poor in equipment, but rich in resources, the drain would be out of an increasing income, or, to put it in other words, a net gain.

Mr. Morman is quite right in his apprehensions concerning the plight of the farmer during the present period of depression, a period by no means past. On the other hand, it is of no use to exaggerate the situation as revealed by the increase in debts. While mortgage indebtedness has increased, so have values. According to the Census report, the ratio of debt to value in 1910 was 27.3%; in 1920 it was 29.1%. This increase can be explained quite adequately. Furthermore, the values of 1910 were more stable than in 1920, thus making a worse showing than appears on the face of the returns for the latter year. Even so, it is hardly reasonable to appear to forget that in-

debtedness is the regular status of the business world. The vital question is not how much a class of people may be in debt, but how easily the debt may be carried; and at present the farmers are not carrying their debts easily. Yet, all things considered, there seems to be no good reason for being unduly pessimistic with respect to the whole question of farm credits.

Despite these few points on which economists may reasonably differ, Mr. Morman has performed a valuable and worth-while task in bringing together such a comprehensive array of facts. In no other single book can a reader find so much of the material that he is likely to want on this subject. In this respect Mr. Morman has contributed a commendable book. In doing so he inspires confidence in the accuracy of his information by his painstaking attention to details, and his care in marshalling the most important facts in a thoroughly clear manner.

B. H. HIBBARD

Schmidt, Louis Bernard, and Ross, Earle Dudley. READINGS IN THE ECONOMIC HISTORY OF AMERICAN AGRICULTURE. *New York: The Macmillan Company, 1925. pp. xii, 591. $3.50.*

THE purposes of this collection of readings are three: (1) to "provide adequate discussion material for courses in the economic history of American agriculture," (2) to "supplement manuals in general economic history on a side relatively underemphasized," (3) to "furnish a much needed historical background for courses in agricultural economics."

For the first purpose the work is undoubtedly excellent; for the second, it affords abundant material from which to select; for the third, it will probably prove as inadequate as selected readings always are for such a purpose: fragments are excellent as fillers but are not satisfactory as background.

The readings are grouped under four headings: (1) Colonial Foundations, 1607-1776; (2) Plantation and Frontier, 1776-1860; (3) Agrarian Revolution and the Settlement of the Far West, 1860-1914; (4) Reorganization and Readjustment, 1914-1924. Many of the selections are taken from the writings of such well-known historians as F. J. Turner, G. S. Callender, P. O. Bruce, C. M. Andrews, F. L. Paxson, J. S. Bassett, Katherine Coman, and Isaac Lippincott; others are from the works of such prominent agricultural economists as B. H. Hibbard, David Friday, J. E. Boyle, E. G. Nourse, M. L. Wilson, and G. K. Holmes; a few are taken from those intensely specialized studies which grow out of theses for the degree of doctor of philosophy, and are full of information but exceedingly dull.

As a whole the work seems better fitted for the advanced student in history who wants to glimpse the economic side of his subject than for the student in agricultural economics who wants the historical side. Like all works of its kind, it lacks continuity; and, while it does very well for the person familiar with the field of history or for one who is willing to do additional reading to bridge the gaps, in the reviewer's opinion it will not provide an adequate historical equipment for the average student in agricultural economics.

MARY L. SHINE

Wood, Edith Elmer. HOUSING PROGRESS IN WESTERN EUROPE. *New York: E. P. Dutton and Company, 1923. pp. viii, 210. $3.*

THIS book is a detailed account of the development of industrial housing

in the principal countries of Europe. The subject is discussed under two main headings: Private Initiative and State Action, respectively, in the countries of Great Britain, Belgium, France, Italy, and Holland.

According to Miss Wood, Great Britain leads the world in housing standards and the steps that have been taken to realize them. Of the other nations of Western Europe, Holland and Belgium most nearly approach the English standards.

The salient feature of the French housing program is the way in which it is linked up with the population problem. In the belief that national safety demands an increased population, rebates on rent are offered to families with four or more children under sixteen years of age. But in spite of a desire to encourage large families, seven- and eight-story tenements are built without elevators, an inconvenience which must be discouraging to family life.

The chapter on Italian housing is perhaps the most interesting in the book. In contrast with the "English cottage in the garden" ideal "for health and for family life," the Italian tendency toward gregariousness expresses itself in the group dwelling. Not only do the working people prefer living in large dwellings, but the architects prefer designing them, while the sociologists, sanitarians, and the leaders of social reform "often make it a matter of patriotism and ethnic loyalty to adhere to what they call the 'millennial traditions of the Latin race.'" Furthermore, in Miss Wood's opinion, the Italians feel a certain prestige in living in a large dwelling in contrast to the English preference for "doll houses."

Housing in Holland is slowly but surely rising to higher levels. In 1901 Holland passed one of the best and the most comprehensive housing laws in any country. This was done after years of deliberation and experimentation. Holland's policy of slow and patient slum clearance is unique. No dwelling is razed until a better one is substituted. Moving into a better dwelling is made a reward, for "the cleanest, most orderly family moves first." One admirable feature of this policy of gradual slum destruction is that it permits individual case treatment and continued supervision of the family. The author gives considerable space to a review of the Dutch appreciation of color and line as revealed in their architecture. Miss Wood is impressed that the Dutch feeling for harmony of color is reflected even in the color of scarfs and caps the children wear, which are of the "same vivid green that adorns their doors." Holland, in the author's opinion, will probably be the first country to have a properly housed people.

The excellence of this book lies in its conciseness and its completeness. It gives in detail the progress and results of private attempts in industrial housing as carried on by philanthropic foundations, public utility societies, social organizations, building gilds, and employers. The garden city movement is one of the experiments being carried on under private initiative. Governmental action takes such ways and means as subsidies, rebates, and loans. The painstaking record of legislative enactments and the abundance of data detract somewhat from the readability of the book. This, however, is more than compensated for by its value as a comprehensive, easily understood source work of the progress of industrial housing in Europe.

GERTRUDE HARLEY

Branson, E. C. FARM LIFE ABROAD. *Chapel Hill, N. C.: University of North Carolina Press, 1924. pp. 303. $2.*

ACCORDING to the introduction to the book, Professor Branson, of the University of North Carolina, spent a full year (1923-1924) in Europe investigating the rural life of Germany, Denmark, and France. He was especially interested in the farm people, their homes, their economic life, their institutions and agencies, and the standard of life. As he traveled he sent letters from the field which were printed in the *News Letter* of the University of North Carolina and five Sunday dailies. These letters were revised and brought together in book form in 1924.

The letters are informal and non-technical, and make delightful reading. Twelve chapters are devoted to Germany, twenty-one to Denmark, and three to France. The author is highly sympathetic with the country life of Denmark, less so with that of Germany, and least of all with that of France. He shows that the farmers of Denmark have lifted themselves agriculturally, educationally, and in business methods, to the highest level reached in any country in the world. Their living conditions are on an equally high plane. The author presents a rather pleasing picture of the rural life of Gemany: its village life, thrift, industry, the love of the out-of-doors.

But when he compares the lot of the peasant women of Denmark with that of farm women of Germany and France, he presents the darker side of the picture. The lot of the French and German farm women is much harder than that of farm women in Denmark or in the United States. If, as the author says, "the final measure of the farm civilization of a country is the lot and fate of the women and children in the farm homes" (p. 265), then the farm civilization of Denmark and of the United States stands higher than that of France and Germany.

Besides furnishing interesting reading, these letters were evidently written to serve still another purpose. In almost every letter Professor Branson contrasts conditions in the United States, but more particularly in North Carolina, with what he sees abroad, and drives home a lesson. The author thereby reveals his own philosophy and beliefs. The statements he makes, without qualifications such as the author might want to make were he writing a book primarily on these questions, are of such a nature that students of American rural life cannot help but challenge them.

For instance, the author bemoans the cityward drift (p. 83) and speaks disparagingly of city life, calling it "a sorry spectacle," "pagan to the core, no matter how we label it, whether Christian or not." Yet (p. 124) he says that one of the troubles of the North Carolina farmers is the lack of a city of the size of Copenhagen to furnish a market for food and feed products. That is why, he says, the North Carolina farmers have to raise cotton and tobacco.

Because of the existence of good urban markets there are few Danish farmers who are ready to sell out and move to town. Yet the author notes a cityward movement in Denmark as everywhere—"in Denmark mainly because the holdings are too small for division among heirs, one of whom may stay on the farm while the rest must go to the cities . . . . or to other countries. It is for this reason that Denmark is already developing areas of static populations, in Fünen for instance, where the census shows no in-

crease of resident inhabitants in 20 years." But the author seems to think that the American rural exodus has other causes, for he continues, "The country exodus in North Carolina and the United States in general is produced by a combination of very different causes. Unless it is promptly and properly checked, the country life of the nation will disappear in another generation or two" (p. 125).

It is true that the crisis in agriculture has accelerated the cityward movement in the United States, but few economists will agree with the author that "the country life of the nation will disappear" for any such reasons. We have a surplus of rural population as well as Denmark, and according to some writers this surplus in North Carolina is so great that the solution of rural problems in that state is to be found in a greater movement towards urbanization. Neither will the author find general support for his statement, "The country civilization of North Carolina and the nation is slated for destruction in the next generation or two unless farm life communities or colonies can begin a rapid development." Colonization of the Durham and Delhi type is going through the acid test now, and it is doubtful if the state of California will go any further with the experiment (pp. 10, 11).

The author makes equally sweeping statements with regard to tenancy. Speaking of Belgium, England, Scotland, and other countries of Europe, he says: "The farmers of those countries are mainly tenants, and in every land farm tenancy means farm poverty soon or late for tenants and landlords alike" (p. 30). "Commercial farming is the last word in farming. It is a kind of farming that is possible to farm owners alone .... never to farm tenants and never to farm regions cursed with wide-spread illiteracy" (p. 106). "The fundamental social ills of North Carolina are excessive tenancy and overweening illiteracy" (p. 107).

The impression is given over and over again that tenancy is one of the fundamental *causes* of farm poverty rather than a symptom of deeper-lying causes. Illiteracy, ignorance, thriftlessness, and lack of industry make certain *forms of land tenure inevitable,* and merely to change the form of tenure changes nothing. Were all the negro tenants, and "croppers" generally, of North Carolina presented with the freehold of a suitably sized farm, the chances are that 75% of them would be landless in 5 years. Given an intelligent, thrifty, and industrious class of farmers, the form of tenure is not as important as it would at first glance seem to be. Farm tenancy in England and Scotland did not mean poverty before the war shook the whole structure of rural England; and if any agriculture could be called "commercial," it was the English agriculture. If one merely recalls the breeds of cattle, sheep, and horses developed on the British Isles under a system of "capitalistic" tenant agriculture, one must be convinced that tenant farming is not necessarily a reason for poor agriculture or poverty.

To strive toward the highest possible owner operation should be our goal; every student of rural life will agree to that. But we will not attain that goal if we confuse causes with effects. Land policies must be shaped with that end in view, but whether the Danish experience should be copied here is another question. Denmark has reduced her percentage of tenancy in a remarkable way, but not without cost. Since 1899, 95 million kroner have

been spent for the purpose of creating 18,000 farm owners, according to the author (p. 232). Although it is said that any reputable farmer over 25 and under 50 years of age can own a farm in Denmark, the farm is not his for the asking. He must have saved at least one-tenth of the purchase price as a first payment. Suppose this were made a condition in the South, how many "croppers" could ever meet that condition? And if they cannot meet it, how will they become farm owners? What will be their status if it is not that of permanent tenants or, worse still, mere farm laborers?

Finally owner operation has been secured at the price of debt, both public and private. "Manifestly, the farmers of Denmark are loaded down with debt," says the author. "Their children and their children's children will be burdened with debt for generations to come. But it is a debt willingly assumed in order to transfer renters of trifling significance into owners and citizens of value and consequence."

In fact, evidence given from the author's own experience would indicate that the system of tenure is of smaller consequence than he holds it to be; for he says that the French farmers are largely owners, yet their standard of life and economic status is far below that of Denmark (p. 272).

G. S. WEHRWEIN

SUMMARIES OF RESEARCH

MULTI-FAMILY HOUSING UNITS AND URBAN TENANCY

A GREAT many factors influence and determine the amount of home tenancy in American cities. This summary is an attempt to determine the significance of the multi-family structure as a factor in this problem. It is an attempt to answer the question, "How much of the tenancy is due to the fact that where multi-family housing is preferred or economical, the opportunity for home ownership is restricted?"

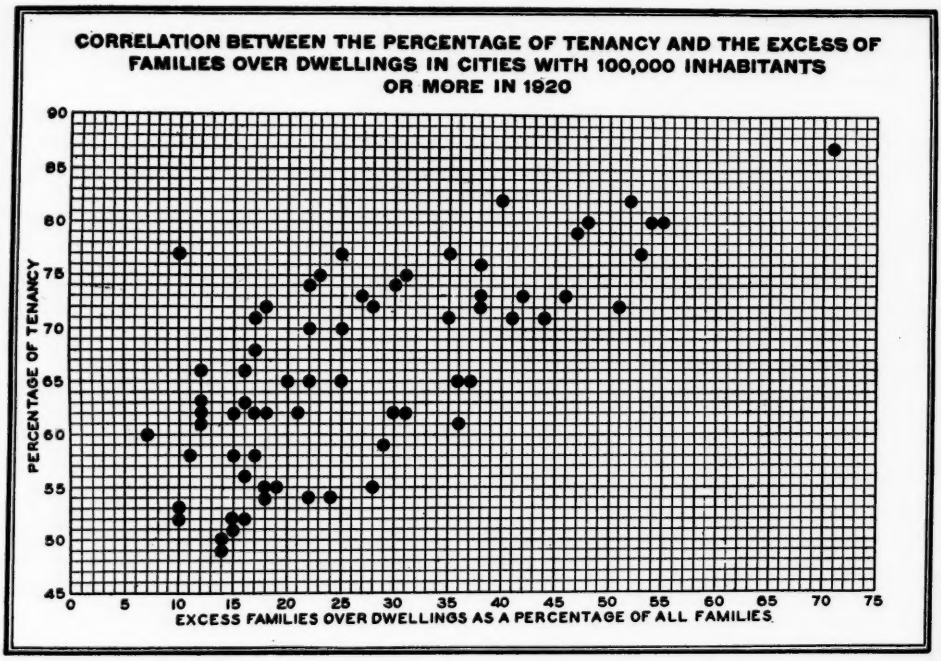
An approximate answer may be found by comparing the percentage of home tenancy in any particular city with the relationship of the number of families to the number of dwellings. When there are two families for every dwelling reported, there would be on the average two families per dwelling. It is not easy or at least customary for more than one occupant to own the dwelling structure. Obviously, the causes back of the demand for multiple structures are the important considerations in determining the causes of the extent and character of urban tenancy, but the extent of multi-family housing is an expression of these causes.

The relationship of the number of families to dwellings is expressed as a percentage excess of families over dwellings and this is compared with the percentage of tenancy. Such a comparison makes it possible to arrive at some conclusions with respect to the importance of multi-family housing and of the deeper causes that lie back of this problem.

In the chart on the following page the 68 cities of 100,000 population or more in 1920 have been plotted according to the above-named factors. Thus New York with 87.3% tenancy and 71.4% excess of families over dwellings is located by counting up 87 places and to the right 71 places. *The extent to which the plottings fall in a diagonal line is an expression of the relationship of these two conditions.*

Cities which are widely out of the line of correlation are Atlanta, Birmingham, Indianapolis, Memphis, New Orleans, Norfolk, and Richmond. It is noteworthy that all of these are southern cities with the exception of Indianapolis. In analyzing these cities no single cause can be assigned as the reason for the high percentage of tenancy. As is characteristic of economic phenomena, there are many factors which are responsible for the high percentage of tenancy in these cities. Recency of growth of a city is important. If the population is made up of a large percentage of young people, there would naturally be a higher percentage of tenancy than in a static city having a larger proportion of the population in higher age groups. Other factors which seem logically to influence home tenancy are commercial conditions, racial differences, permanence of employment, climate, and even living customs. These factors working hand in hand prevent a universal correlation between excess of families over dwellings and tenancy. It should be remembered, however, that the prevalence of multi-family structures is only one of many factors affecting tenancy.

The extent of multi-family housing



appears, however, to bear a close relation to the amount of tenancy. Barring the above-mentioned southern cities, the relationship appears rather close. In fact, including these cities, whose geographic location seems to have an influence, the correlation between the rank of the cities on the basis of percentage of tenancy and percentage of excess of families over dwellings is 68.2%, a fairly high correlation for phenomena of this character. Seemingly, the extent and popularity of the multi-family structure is an important cause of the extent of urban tenancy.

As long as there is a marked preference for multi-family structures in large cities for reasons of economy, an increasing percentage of urban home tenancy in the United States may be expected. Two present tendencies indicate that this trend of tenancy may be checked or slowed down. One contingency is that the system of cooperative ownership, already so prevalent in Europe, may become common in this country; the other possibility is the accelerated movement of urban population to suburbs where recent building statistics show greater activity in constructing one- and two-family dwellings.

GERTRUDE HARLEY

DIVIDEND RECORD OF GAS UTILITIES

THE growing financial importance of the gas utilities in the United States may be evidenced by a general survey of the dividend rates paid by these companies during the past several years. In compiling the data concerning dividends, the reports of the gas utilities in the 1924 volume of

TABLE I. ANALYSIS OF DIVIDEND PAYMENTS ON COMMON AND PREFERRED STOCK OF GAS UTILITIES, 1907-1923*

	COMMON STOCK							PREFERRED STOCK						
Year	No. of Companies Reporting	No. of Companies Paying	Per Cent of Companies Paying	No. of Companies Not Paying	Per Cent of Companies Not Paying	Average Rate of Companies Reporting	Average Rate of Companies Paying	No. of Companies Reporting	No. of Companies Paying	Per Cent of Companies Paying	No. of Companies Not Paying	Per Cent of Companies Not Paying	Average Rate of Companies Reporting	Average Rate of Companies Paying
1907	82	35	42.7	47	57.3	3.52	7.23	27	22	81.4	5	18.6	5.56	6.02
1908	87	41	47.1	46	52.9	3.49	7.04	30	25	83.4	5	16.6	5.22	5.78
1909	87	41	47.1	46	52.9	3.30	7.23	32	26	81.2	6	18.8	5.08	5.79
1910	93	44	47.3	49	52.7	4.24	8.60	35	29	82.9	6	17.1	5.21	5.67
1911	100	48	48.0	52	52.0	3.73	8.31	43	35	81.4	8	18.6	4.54	5.07
1912	114	57	50.0	57	50.0	3.88	7.74	45	37	82.2	8	17.8	4.95	5.53
1913	115	58	50.4	57	49.6	3.76	7.41	44	37	84.1	7	15.9	5.48	5.69
1914	120	58	48.3	62	51.7	3.55	7.62	44	37	84.1	7	15.9	5.55	5.76
1915	121	55	45.4	66	54.6	3.84	8.40	45	37	82.2	8	17.8	5.54	5.91
1916	127	62	48.8	65	51.2	3.84	10.18	46	38	80.4	8	19.6	5.73	6.12
1917	130	62	47.7	68	52.3	3.37	7.35	45	38	84.5	7	15.5	5.70	6.20
1918	132	58	43.9	74	56.1	3.10	7.24	46	36	78.7	10	21.8	5.33	5.96
1919	135	54	40.0	81	60.0	2.94	8.42	47	37	78.6	10	21.4	5.30	5.90
1920	137	54	39.4	83	60.6	3.04	6.92	46	35	76.0	11	24.0	5.13	5.93
1921	139	61	43.8	78	56.2	3.19	6.93	45	35	77.8	10	22.2	5.35	5.98
1922	141	68	48.2	73	51.8	4.18	7.91	49	38	77.5	11	22.5	5.14	6.25
1923	146	71	48.6	75	51.4	4.04	9.33	53	38	71.6	15	28.4	5.25	6.36

*Data based on Moody's *Analysis of Public Utility Investments.*

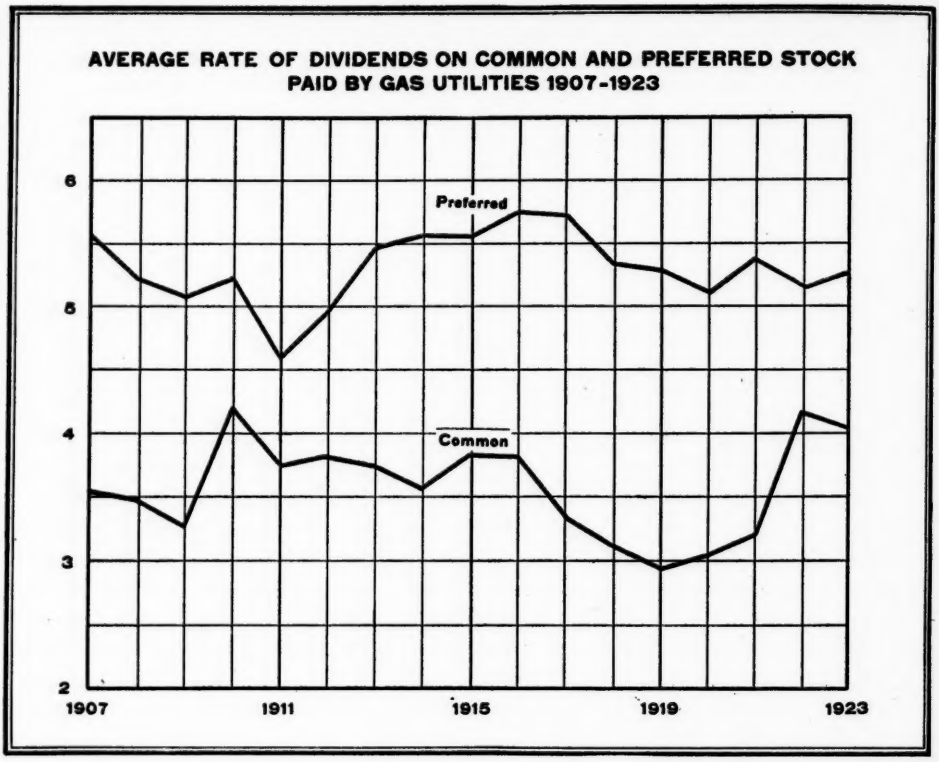
Moody's *Analysis of Public Utility Investments* were taken as a fair sample of companies throughout the country. No gas-electric companies or natural gas companies are included in the data, since such companies would not be truly representative of the gas industry. Companies whose stock is held by holding companies, or whose dividend records are not complete, are also eliminated; so the total number of companies included in the data for 1923 is 146 having common stock and 53 having both common and preferred. The number of gas companies on which this analysis is based has increased steadily since 1907, the starting point of this study, as the above table shows.

The percentage of these companies that paid dividends on common stock of any rate moves gradually upward from 42.7% in 1907 to 48.6% in 1923. During this period, however, there was a decline from 1916 to 1920, when a low point was reached. In that year 39.4% of the 137 companies reporting paid dividends on common stock. In the years 1919 and 1920 gas utilities suffered the most. From 1920 to 1923 the ratio of companies paying to all companies reporting rose rapidly.

A similar ratio with respect to preferred stocks, although naturally much higher, has not increased correspondingly. While 81.4% of the companies paid dividends in 1907, only 71.6% paid in 1923. This decline is partly accounted for by a slower rise from the low period of 1920, and also by the fact that several companies initiated preferred stock dividends in 1923, though the initial dividend was not paid.

Two average rates for both common stock and preferred stock are tabulated. One is the average rate of all companies reporting, while the other is the average rate only of companies paying dividends. Neither of these rates is an absolutely true indicator, because in the first average are included newly organized corporations which ordinarily would not be paying dividends during the first years of organization (especially in the case of common stocks), and in the second average, older companies, which should be included, are left out.

The average dividend rate on com-



mon stock of all companies reporting, outside of a low mark of 2.94% in 1919, reached 4.18% in 1922, the highest point since 1910. Although this rate dropped slightly in 1923, the rise in the ratio of companies paying dividends shows that the drop in dividend rates is probably due to the addition of new companies. The average rate on common stock of companies paying dividends shows a corresponding increase through 1923, and a similar depression in 1920. The sudden jump, in 1916, to 10.18% is due to a large increase in the dividend rates of several companies, and the declaration of extra dividends. In order to get a fair idea of the actual trend of dividend rates, however, both average rates should be considered.

The average dividend rates on preferred stock show only a small fluctuation, which may be attributed chiefly to the character of the security. The average rate on the preferred stock of all companies corresponds closely with the average rate on preferred stock of companies paying dividends, the latter remaining between .5% and 1% higher than the former throughout the period of analysis.

The chart on this page pictures the trend of the average dividend rates on common and preferred stock of all companies reporting. In the curve representing the rates on common stock, the depression of the war period and the rapid pick-up in 1922 and 1923 are very noticeable.

W. G. MAAS

COMMENTS ON LEGISLATION AND COURT DECISIONS

JUDICIAL STATUS OF ARBITRATION OF PUBLIC UTILITY LABOR DISPUTES

SINCE regulation of public utilities was first established in this country, public policies pertaining to labor relations in these industries have gone through an almost complete cycle from governmental inaction to compulsion and back again toward the starting point.

The successive policies in this cycle on the steam railways may be thus summarized: (1) Unrestricted and unaided bargaining between managements and employees until 1888; (2) Provision for voluntary arbitration in Act of Congress, 1888, but neither employees nor carriers availed themselves of the act; (3) Temporary voluntary arbitration boards under the Erdman Act of 1898, although this machinery was not used until 1907, when concerted wage movements on the part of the train-service brotherhoods began; (4) Permanent board of mediation and conciliation, with voluntary arbitration as a last resort, under the Newlands Act of 1913; (5) Compulsory arbitration by Congress in the Adamson law of 1916; (6) "Bargaining" with the government during the period of federal control; (7) "Compulsory conference" and permanent voluntary arbitration under the Transportation Act of 1920.

Public policies of dealing with labor relations on the local utilities have in the main relied on machinery for mediation and conciliation, with possible voluntary arbitration when disputes were not successfully adjusted by the parties themselves. Notable exceptions to this prevailing policy are the Kansas Court of Industrial Relations embodying compulsory arbitration, and the Colorado compulsory investigation system.

As a result of four decisions[1] of the United States Supreme Court during the past two years, doubt has been cast upon the effectiveness of the policies illustrated by the Kansas Court and the Railroad Labor Board. The effect of these decisions is likely to be such as to bring about a reopening of the entire question of the proper sphere of public and private initiative in the adjustment of labor disputes on public utilities. If this is done, the alignment of forces and the temper of the times may result in a return to the policy of *laissez-faire* which prevailed in the early days of public utility regulation.

In view of this eventuality, it is significant to examine the legal status of compulsory arbitration of the Kansas type and voluntary arbitration after the Railroad Labor Board pattern in the light of these recent decisions.

The Kansas Court

Chief Justice Taft in the first Wolff Packing Company case gave the opinion

[1] *Wolff Packing Co.* v. *Kansas Court of Industrial Relations*, 262 U. S. 522 (1923); *Wolff Packing Co.* v. *Kansas Court of Industrial Relations*, 45 Sup. Ct. 441 (1925); *Pennsylvania Railroad Co.* v. *U. S. Railroad Labor Board*, 261 U. S. 72 (1923); *Penn. System Federation No. 90* v. *Penn. R. R. Co.* 45 Sup. Ct. 307 (1925).

of the court that the compulsory fixing of wages in the plant in question infringed the liberty of contract guaranteed by the Fourteenth Amendment. The fundamental principle which the court affirmed was that compulsory arbitration of wages and prohibition of strikes was an invasion of freedom to contract that could only be justified under "exceptional circumstances." In the case before it, these "exceptional circumstances" did not exist. There was no present or impending strike which would result in a general cessation of food production or distribution; the term of the Industrial Court's award was of indefinite, not temporary duration; the Wolff Packing Company was a competitive enterprise, and not a monopoly; in short, the public interest in the continuous service of this company was not so great as to require such a drastic invasion of private rights. The substance of the court's opinion was that the nature of the business determines how far the state may go in using compulsion in the settlement of wage disputes.

The words of the court are significant: "It *involves a more drastic exercise of control* to impose limitations of continuity growing out of the public character of the business upon the *employee than upon the employer;* and without saying that such limitations *upon both* may not be sometimes justified it must be where the obligation to the public of continuous services is direct, clear, and mandatory and arises as a contractual condition express or implied of entering the business either as owner or worker. It can only arise when investment by the owner and entering the employment by the worker create a conventional relation to the public somewhat equivalent to the appointment of officers and the enlistment of soldiers and sailors in military service." [2]

This extreme comparison and the general tenor of these words, if interpreted literally, convey the impression that compulsory arbitration would be a justifiable policy only in the case of governmental employees. However, when one compares these words with the language of previous decisions, it appears entirely possible that the court might uphold compulsory arbitration in the case of railways, other common carriers, and other public utilities, all subject to the strictest regulation of rates and service. A further impression is that compulsory arbitration is less likely to be upheld when applied to "exceptional occupations" recognized as public callings from earliest times by force of inertia, or when applied to businesses which, though private at their inception, have become affected with a public interest through changed economic conditions. Even when the scope of this policy is thus narrowed, there is room for doubt whether the court would uphold a delegation of the power to arbitrate *compulsorily* to a subordinate, permanently sitting board. At least in the case before us the court took pains to point out that the Adamson law [3] involved arbitration by the legislature itself rather than by a subordinate board.

These impressions, however, are implied from the dicta in the Wolff case, compared with the court's attitude in *Wilson* v. *New*. In the Wolff case these issues were not specifically joined. Hence, one can only say that the validity of the Kansas type of compulsory arbitration is possible, though not wholly probable, when applied to wage disputes

[2] 262 U. S. 522 at 541. Italics mine.

[3] Upheld in *Wilson* v. *New*, 243 U. S. 332 (1917).

on public utilities. The Kansas legislature erred, it is certain, in attempting to class with public utilities a competitive enterprise like a packing company for the purpose of regulating wages. It is not unlikely that this blow to the prestige of the Industrial Court will impair its effectiveness in dealing with disputes affecting recognized public utility services, when they arise in the future.

The second Wolff Packing Company case [4] differed from the first mainly in the fact that it involved hours rather than wages. The Supreme Court merely reaffirmed its earlier decision and extended its scope to include the compulsory determination of hours of work. The net result seems to be the further deterioration of the Kansas Court.

The Railroad Labor Board

The effectiveness of voluntary arbitration in the national utility field was at stake in the Labor Board and Pennsylvania cases. Although the Board's representatives appeared before the court only in the first case, the underlying issue in both was the scope of the Board's powers under the Transportation Act of 1920.

The earlier case established the Board's right to make public a decision against the desires of a railway company and also to publish the fact that the company refused to comply with the Board's decision. The issue arose as a result of the Pennsylvania Railroad Company's policy not to deal with the representatives of certain unions unless these representatives were employees of the road. The aggrieved unions complained to the Board that the railroad refused to give an opportunity for its employees to vote for their union agents as representatives in conference with the management. The Board prescribed a form of ballot which allowed votes to be cast for a union as employee representative. The Pennsylvania road declined to obey, and organized what is popularly known as a "company union."

The fundamental conflict between the Board and the carrier was their differing views as to whether Congress, in imposing a duty to confer, meant to enact a policy of collective bargaining with trade unions.

The court did not, of course, presume to decide specifically this question of policy. That decision was properly within the discretion of the Board as was also the question of publication of awards and non-compliance with awards, after authority to use discretion had been sustained by the courts.

In the second case [5] the Supreme Court was even more explicit in construing the labor provisions of the Transportation Act. This case was brought against the railroad by the same aggrieved unions in an effort to get the courts to do what the Railroad Labor Board had no power to do, namely, compel recognition by the carriers. As Chief Justice Taft says: "What complainants (unions) here are seeking to do is to enforce by mandatory injunction a compliance with a decision of the Board, not based on the legal rights of the parties, but on its judgment as to what legal rights the disputants should surrender or abate in the public interest and in the interest of each other, to maintain the harmonious relations between them necessary to the continuance of interstate commerce, and to avoid severing those relations as they would have a strict legal right to do. Such a remedy by injunction in a court it was

[4] *Wolff Packing Co.* v. *Kansas Court of Industrial Relations*, 45 Sup. Ct. 441. (1925).

[5] *Penn. R. R. System Federation No. 90* v. *Penn. R. R.* 45 Sup. Ct. 307 (1925).

not the intention of Congress to provide." [6]

The reason for the court's refusal to uphold the hands of the Labor Board was simply that "there is nothing compulsory in the provisions of the statute as against either the company or the employees upon the basis of which either acquired additional rights against the other which can be enforced in a court of law." The Pennsylvania Railroad may "refuse to comply with the decisions of the Labor Board," in the matter of employee representation, and "thus defeat the purpose of Congress," and still be "within its strict legal rights." "We do not think Congress, while it would deprecate such action, intended to make it criminal or legally actionable." [7]

In other words, the "duty to confer," in the Transportation Act, is a moral duty, not a legal duty, and the Railroad Labor Board is supposed only to formulate and publish the moral duty, which no public agency can at present enforce. It is futile to imagine that public opinion can effectively register its disapproval of any labor policy of management by refusing to patronize the road. Public opinion is generally nebulous and ineffective unless crystallized by some representative agency with real administrative power. As long as either carriers or employees may disregard with impunity the decisions of the Labor Board, it is difficult to see how the Board can in practice do more than merely mediate and conciliate, unless both parties agree to arbitrate. If this is the alternative, then we have a reversion substantially to the policy of the Newlands Act.

The reversion to the policy embodied in the Newlands Act may be determined definitely if a current controversy between the Labor Board and certain train service brotherhoods finally reaches the stage of adjudication by the Federal Supreme Court. In this dispute the unions refused to testify before the Board. If the Supreme Court should decide that the Board may not compel testimony, then clearly the Board would be nothing but a conciliatory body.

Nature of the Problem

When policies of voluntary and compulsory arbitration are thus returned to legislatures for revision, the question will naturally be raised: "What next?" Most of the unions would probably prefer bi-partisan adjustment boards such as those functioning during the period of federal control. Many of the executives would prefer to be left alone. But from the public standpoint is it desirable to limit public interference in labor disputes to conciliation and occasional arbitration? Past experience with this policy has not been altogether satisfactory. Should we, therefore, go back to the policy of public inaction and *laissez-faire* prevailing before 1888? If legislatures in despair feel inclined to take this path, they should consider well what may be the public consequences of a "do-nothing" policy.

The essence of such a policy is to leave wholly to the managements the responsibility of so arranging their labor relations as to induce efficient and continuous service on the part of their employees. At the present time two steam railways afford good illustrations of what may be expected from giving free rein to management. Before any legislative body starts forth on a new tack, it might prove helpful to examine with care the relative success of these

[6] 45 Sup. Ct. 307 at 311.

[7] *Ibid.*

two opposite policies of "company unions" and of cooperative dealing with trade unions. The Pennsylvania Railroad is the outstanding adherent of the former policy, the Baltimore and Ohio of the latter. Which of these two policies yields the best results in the long run is of prime interest to other carriers and to the public as well.

The relinquishment of any measure of public regulation of labor relations places heavy obligations upon public utility managements. They already are obligated to give continuous and efficient service at regulated rates. No such obligation legally rests upon labor. For the most part under our theory of regulation we control income but not expenditures. Thus in those dealings with consumers that affect income, public utility managements function in a restricted, although more or less protected, market. But in those dealings that affect expenses, whether of labor or materials, they compete with ordinary private enterprise. In the one case the market is regulated, in the other competitive. It may appear logical to regulate both the flow of income and the ebb of expenditures, but from the standpoint of public policy if we begin by regulating wages, how can we avoid going further and regulating expenditures for rails, ties, cars, and equipment—a conclusion which in the present state of opinion appears absurd. Moreover, as far as regulated expenditures for labor are concerned, three things stand in the way—custom, the Thirteenth Amendment, and the rights of labor as "found" by courts.

Unless this judgment of society is radically changed, it is likely that the whole question of public and private labor policies of public utilities will be reopened and reformulated in the near future. A determining factor in the outcome will be the relative bargaining positions of managements, employees, and public. Yet bargaining power is affected by the degree of responsibility felt by the three interested groups. Organized labor in public service industries is increasingly feeling that the use of the time-honored weapon of the strike immediately arouses public disapproval. Short of complete public regulation, representative public agencies feel that something must be done to prevent disruption of service; yet the prevailing tendency, as reflected in judicial decisions, is to curb public initiative.

Is it a reasonable alternative to leave the responsibility wholly or mainly on management? Three conditions appear essential for the success of such a policy: (1) Public understanding of, and sympathy for, the difficult positions of both management and labor; (2) Labor's recognition that cooperation in serving the public is a more statesmanlike and profitable policy in the long run than conflict; (3) A disposition on the part of public utility executives to realize that their especially close relations to the public obligate them to set an example, not follow one, of scientific and progressive labor policies. Public service industries should lead in this respect rather than remain content with a rank-and-file position.

Understanding and "sweet reasonableness" on the part of the public, statesmanship on the part of labor, leadership on the part of management —these three, and, to the present writer, the last-named principle seems fundamental. Yet it will be generally helpful to recall that the labor policies of public utilities are different and more difficult in many respects than similar policies in industries not obligated to give continuous service.

E. W. Morehouse

THE EXEMPTION OF HOMESTEADS FROM TAXATION

THE marked increase in tenancy in recent years along with the tremendous increase in the tax burden has prompted certain groups in the community to seek a legislative remedy for both ills in what is known as "homestead exemptions." The theory underlying homestead exemptions is that a lightening of the tax burden will make it financially easier, and, therefore, more attractive, for people to acquire ownership of city and farm homes.

Such a law was passed by the Wisconsin Legislature in 1923, has been in operation since January 1, 1924, but has recently been repealed by the 1925 legislature, with the approval of the governor. Why was this speedy reversal of policy decided upon? Aside from any political considerations, is not the cause to be found in the economic effect of homestead exemption?

The Wisconsin law, stated briefly, exempted: "All buildings and improvements upon any parcel of land owned and used as a homestead as defined in section 2983 of the statutes not exceeding $500 of the value of such buildings and improvements, if the owner of the homestead has filed an affidavit with the assessor on or before the first day of July of the year in which the assessment is made claiming exemption under the provisions of this subsection."

In order to form a judgment of the economic effect of this law, a small study was made of its operation in what was considered a fairly representative township in Dane County—the town of Albion. At the same time the possible effect of more sweeping exemptions was also studied for comparative purposes. Also included in the study as having a bearing upon the central problem, the distribution of state and county tax burdens between urban and rural districts in Dane County was analyzed cursorily.

In view of the fact that this law was in operation for such a short time, it would be unfair to conclude that this study represents the "actual" effect of homestead exemption upon the distribution of local tax burdens. At the most, therefore, the conclusions are the reasonably probable or "possible" effects under fair assumptions.

The Assumptions and the Method

The chief assumption is that Albion, in Dane County, represents a typical taxing district in Wisconsin. Since agricultural districts predominate in Wisconsin, the selection of Albion can be justified if it is a typical agricultural township. It has some of the best as well as some of the poorest land in the county; it exhibits considerable variation in size and value of properties; and it has a small unincorporated village. These characteristics, it was felt, furnished enough diversity to justify its selection as a type. Other assumptions will be apparent as the method of study is briefly outlined.

All parcels of real estate in Albion were assembled into operating units with the aid of the 1922 tax rolls and a plat map of the township. Unimproved properties that were located at a considerable distance from the improved property of the owner were classified as unimproved, although probably a few of the properties so classified were really operated in connection with some distant improved property. This fact would not affect the conclusions of this study, inasmuch as the improved units were classified without regard for the unimproved parts.

All possible homesteads were then classified into five groups according to size (as shown by value) and into a sixth group, called non-homestead, were put all commercial and unimproved properties and any others that could not claim exemption under the law.

It should be remembered that the law defines a homestead as a property occupied by the owner. However, the percentage of tenancy is not the same in any two taxing districts, nor is it the same in each size group of properties in any one taxing district. In order to avoid any difficulties occasioned by this lack of uniformity and also to provide a broad basis for generalization, home ownership was assumed to be 100% in Albion. In other words, the assumption was made that all improved properties classified as homesteads could claim exemptions. This assumption is, of course, a deviation from actual facts and can be justified only by a desire to arrive at general conclusions that will be typical in all respects other than the degree of tenancy.

In computing the redistribution of tax burdens, it was assumed that the aggregate amount to be raised by taxation remained constant. As a matter of fact, this amount would increase or decrease according to the budgets approved by the governing body of the taxing district, but obviously this uncertainty had to be discounted in this study.

Another important detail of the Wisconsin system of raising revenue, which must be kept in mind, is the fact that there are four distinct levies—for the state, the county, the township, and the school district. It was in some of the school districts that the economic effect of the $500 homestead exemption was most keenly and immediately felt; and as the governor stated, it was largely due to this fact that the law was repealed. Some school districts found that the exemption removed from the tax roll such a large portion of the taxable property that sufficient funds could not be raised for school purposes. In other school districts, in which there is a large proportion of urban residential property, an undue share of the school tax was shifted upon rural property.

Because of the wide variation in the character of school districts in regard to the kind of property and the amount of school taxes levied, and because of the fact that school taxes constitute less than half of the total tax levy, it was considered desirable to trace in this study the effect of homestead exemptions upon the distribution of all taxes other than school taxes. It is recognized that any given school district will be subject to an additional effect upon the distribution of school district taxes —depending upon the character of the district. This additional effect, it appears from the Governor's statement in signing the repeal, was the chief cause of dissatisfaction with the law. However, the township was used as a basis for this study because a typical township is more easily discovered than a typical school district.

Finally, this study was broadened to include not only the possible effect of the $500 exemption of the law, but also the possible effect of three higher exemptions.

The Redistribution of Tax Burdens (Other than School Taxes) between Various Sized Groups of Property

1. *By a $500 homestead exemption.* Any reduction in assessments in a taxing district must necessarily result in an increased tax rate or a reduction in the

EXTENT TO WHICH VARIOUS PROPERTY GROUPS WOULD BE AFFECTED BY $1,000, $2,000, AND $3,000 EXEMPTIONS

Size Groups	$1,000 Exemption		$2,000 Exemption		$3,000 Exemption	
	Increase of Tax	Decrease of Tax	Increase of Tax	Decrease of Tax	Increase of Tax	Decrease of Tax
Less than $5,000	.....	40.0%	.....	55.2%	.....	53.6%
$5,000 to $10,000	.....	6.1%	.....	9.7%	.....	8.1%
$10,000 to $15,000	.....	0.01%	.....	1.1%	.....	2.3%
$15,000 to $20,000	1.9%	.....	2.1%	.....	0.6%	.....
$20,000 and over	4.2%	.....	7.1%	.....	7.8%	.....
Non-Homestead	8.3%	.....	15.7%	.....	21.2%	.....

amount of taxes levied. Since the desired tax revenues are presumed to be constant, a $500 homestead exemption, under the assumptions made, relieves all homestead properties valued at less than $5,000, of 23.4% of their present local tax burden. In the case of properties valued between $5,000 and $10,000, the tax burden is lightened by 3%. But properties between $10,000 and $15,000 in value have *increased* tax burdens of .2%; similarly, properties valued between $15,000 and $20,000, and those above $20,000, have increased burdens of 1.1% and 2.2%, respectively. The sixth group of properties, classed as non-homestead, have an increased burden of 4.2%.

2. *By $1,000, $2,000, and $3,000 exemptions.* The table on the following page indicates the extent to which the various property groups would be affected by the above-mentioned exemptions.

3. *General conclusions from the above computations.* Four general conclusions may be drawn:

(*a*) The percentage *decrease* in the tax burden upon small properties is large compared with the percentage increase in the case of other groups of properties.

(*b*) The properties affected most adversely are those valued at over $20,000 and the non-homestead properties.

(*c*) The tax burden upon properties valued between $10,000 and $20,000 remains practically the same regardless of the size of the exemption.

(*d*) If the sole purpose of the exemptions is to encourage home ownership on the part of the small property owners, the $2,000 exemption gives this group the maximum benefit. If the exemption is raised beyond $2,000, a part of the tax on larger properties works back upon the smaller properties because of the smaller amount of improvements on the small properties. It must be remembered that these conclusions apply to all taxes other than school taxes.

In addition to these conclusions, it may be well to state that one-fourth of the properties in Albion are in the group valued at less than $5,000, and would, therefore, be benefited in a substantial measure by any of the above-mentioned exemptions. It is also true that almost half of the properties would be practically unaffected, since these properties are in the $10,000-$20,000 group.

It appears, therefore, that the present law accomplishes in a general way what its advocates sought.

It should be remembered, however, that these conclusions apply to an agricultural district in which the total as-

sessed valuation of both small and non-homestead properties is small compared with the total assessed valuation of other classes of property. In a community where approximately the same ratio exists between the total assessed valuation of the various groups of property, the same results can be expected from homestead exemptions. On the other hand, in a community where the total assessed valuation of small properties is large compared with that of non-homestead and other groups of properties, the effects would be the reverse—the relief to the small property owners would be small in comparison with the increased burden upon the non-homestead group. Probably the proportions of various sized groups as revealed in this study generally prevail.

The effect of this exemption upon the distribution of the local tax between farmers and urban property owners depends entirely upon the character of each taxing district. In a town like Albion, where most of the small properties are owned by farmers, practically the only shift of the burden is between property groups and not between classes. However, in any unincorporated town, where there is a much larger amount of residential property owned and occupied by city people, the tax burden would be shifted to the large farm properties and non-homestead properties.

The Redistribution of State and County Tax Burdens between Various Counties, Townships, Cities, and Villages

The shift of the state and county tax burden between districts depends upon the ratio of both the total assessed valuation of property and the number of owned homes in one district as compared with another. In Dane County, for example, if all owned homes claimed the $500 exemption, there would be practically no shift of the state and county tax burdens between urban and rural districts, because the number of owned homes and the total assessed valuation of property are very nearly the same in both urban and rural taxing districts. In a strictly agricultural county, however, the urban districts would pay a part of the tax that is now paid by the rural districts, and *vice versa* in the case of a predominantly urban county.

The shift of state taxes among various counties as a result of homestead exemption is relatively insignificant, but operates generally according to the same rule governing the shift of state and county taxes among districts.

Summary

It is no part of the purpose of this study to consider the desirability of homestead exemption from the standpoint of public policy. Our aim has been merely to examine the economic effects of this policy.

The popular theory is that homestead exemption reduces property taxes. This is not true. What really results from homestead exemption is a redistribution of tax burdens, such that some property owners are relieved while others have increased burdens. In a typical community in Wisconsin, this redistribution tends to benefit small property owners and penalize those who by thrift or otherwise have accumulated property of greater than average value. Increasing the exemption, however, reaches a point of diminishing returns when the increased burdens on the larger holdings tend to work back upon the smaller properties.

Another phase of the theory underlying homestead exemption deserves a detailed and critical examination which cannot be given here. That is the whole question of the effect of taxation upon land utilization. The advocates of homestead exemption claim that this policy will discourage the holding of unimproved land and encourage tenants to rise to the status of ownership. The opponents of this policy assert that most unimproved land remains unused because general economic conditions are not such that the land can be used profitably, and that if the use of this land is artificially stimulated by homestead exemption, not only the new homesteader but the whole community will eventually suffer from overexpansion. These opposite assertions concern the general problem of the relative burdens of taxation upon property, upon various forms of property (agricultural, industrial, commercial, and residential, as well as real and personal property), and upon incomes. It may be that taxes upon property as a whole or upon particular classes of property are discouragingly heavy compared with taxes upon income.

It can hardly be maintained that the Wisconsin experiment with homestead exemptions conclusively proved either one side or the other of the question of the effect of taxation upon land utilization; the experiment was too brief. If any economic reason can be assigned for the abandonment of the exemption policy, it was probably a realization on the part of the legislators that homestead exemption meant a redistribution, rather than a reduction of tax burdens, and that the decreased burdens on small property holders were more than offset by the increased burdens on other classes of property.

O. M. JOHNSON
B. W. ALLIN

COMMERCE CLEARING HOUSE

Federal and State Income and Inheritance Tax Services

NEW YORK
120 Broadway

CHICAGO
Ill. Merchants Bk. Bldg.

WASHINGTON
815 15th Street N. W.